IN THE

Supreme Court of the United States

OCTOBER TERM—1951

No. 360

NATHAN KATZ, individually and suing on behalf of himself and all other common stockholders of R. HOE & CO., INC., similarly situated,

Petitioner,

v.

R. HOE & CO., INC. *et al.*,

Respondents.

REPLY BRIEF OF PETITIONER

POINT I

"The right to be a freeman of a corporation is a valuable temporal right. It is the right of voting and acting in the corporate concerns, which the law recognizes and enforces, and for the violation of which it provides a remedy. It is founded on the same basis as the right of voting in public elections: it is a sacred right" (Story, J., in *Dartmouth College* v. *Woodward*, 4 Wheat. 518, P. 701).

Recognizing that the Hoe Plan of Readjustment, approved by the decree of the United States District Court for the Southern District of New York in 1935, is the fount

of the voting rights and contractual obligations *inter sese* of its respective classes of stockholders, Respondents call attention to "The extraordinary limitations and restrictions imposed upon the common stock by the Federal Court Receivership" (Headnote p. 7, Res. Br.). Respondents assert: "It thus appears that not only were all voting rights (*with immaterial exceptions*) vested in Class A stock but the common stock was 'specifically excluded' from voting on a consolidation pursuant to section 86, as well as from the right to vote 'for establishing priorities or creating preferences' pursuant to section 36, now 35" (Resp. Br., 8; italics added).

It is with these class voting rights of the common stockholders, lightly brushed aside by Respondents as IMMATERIAL EXCEPTIONS, which were vested in the common stockholders by the Plan of Readjustment, in Bankruptcy, that we are here concerned: *i.e.*, the right of cumulative voting in the election of directors; the right to vote on any amendment to the corporate charter affecting the election of directors; and the right to elect six out of eleven directors, once the arrears on the "A" stock were eliminated; in short, the right to take control of the debtor from the "A" stock, by means of the corporate elective process. For this, the common stockholders had been waiting fifteen years, at the time that the plan of consolidation was effectuated in 1950.

Fully a century before *Dartmouth College* v. *Woodward*, 4 Wheat. 518 (U. S. 1819), was decided by this Court, Lord Holt had settled the doctrine that voting rights in corporate elections were vested property rights. Justice Story, writing in *Dartmouth College* v. *Woodward*, says at page 701:

> "The right to be a freeman of a corporation is a valuable temporal right. It is the right of voting and acting in the corporate concerns, which the law recognizes and enforces, and for the violation of which it

provides a remedy. It is founded on the same basis as the right of voting in public elections; it is a sacred right; and whatever might have been the prevalence of former doubts, since the time of Lord Holt, such right has always been deemed a valuable franchise and privilege. Lord Holt says * * * Where the privilege of election is used by particular persons, it is a particular right vested in each particular man."

The cumulative voting right of the Hoe Common Stock in the election of directors; its origin and nature as a vested property right.

Mandatory Cumulative Voting first appeared in the Illinois Constitution in 1870. Since then, seventeen states of the Union have made similar provision in their constitutions. In *Looker* v. *Maynard,* 179 U. S. 46 (1900), it was settled by this Court that the State of Michigan had the right, under its reserved power, to so amend its laws as to make cumulative voting mandatory upon corporations organized before enactment of the amendatory statute.

Cumulative voting has also since 1870 become optional in seventeen states of the union, including New York. It is in this category that the rights of the stockholders of R. Hoe & Co. Inc., have been placed by the Plan of Readjustment in Bankruptcy, promulgated in 1935, by the Debtor Hoe, and voluntarily accepted by a majority of the holders of both classes of its stock, the "A" and the common. The source and nature of these cumulative voting rights are set forth in the Appendix to the Petition for a Writ of Certiorari (Pet. pp. 37-42), and they have not been disputed by the Respondents.

We are concerned, therefore, with the following contractual obligations voluntarily assumed by the Debtor Hoe in the Plan of Readjustment dated January 16, 1935 and fully accepted by the "A" stockholders and the common

stockholders alike: "All voting for directors will be cumulative * * * and provided further that *except with the consent of the majority of the common stock,* no amendment of the Certificate of Incorporation shall be made which shall impair the right of the Common Stock voting as a class to elect and continue in office two members of the Board of Directors as such Board shall be constituted from time to time." (Italics added.)

By the specific terms of Section 77B, sub. p. of the Bankruptcy Act as amended (48 Stat. 912), it is provided that this Plan of Readjustment "shall apply as fully to debtors (and their) stockholders * * * whose interests * * * have been acquired prior to that date (June 7, 1934) as to debtors (and their) stockholders * * * whose interests * * * are acquired after that date."

Petitioner therefore, took the restrictions and limitations on voting rights, as well as his cumulative and other voting rights, from the Plan of Readjustment in Bankruptcy, the moment he acquired his shares in December 1949. These voting rights and limitations are necessary concomitants of each other.

POINT II

"One gathers that the cumulative voting privilege when once accorded, cannot be taken away except by authority equal in grade to that by which the privilege was conferred" (Bowes & de Bow, Minn. Law Review, 1937, Vol. XXI No. 4, p. 351).

(a) **When Mandatory;** It is logical to assume that the right to grant cumulative voting under a constitutional reservation of power, is coextensive with the right to revoke such provision, whether founded on legislative enactment or constitutional provision; and that is the clear inference to be drawn from this Court's decision in *Looker* v. *Maynard, supra.* That proposition has only a peripheral interest in this case.

(b) **When Optional** by state statute, it has been the settled law, in New York and other jurisdictions alike (prior to the decision of the present case) that cumulative voting rights cannot be abrogated, except by authority equal in grade to that, by which the privilege was conferred.

Thus in New Jersey Chancery Court, in the case of *Loewenthal* v. *Rubber Reclaiming Co.,* 52 New Jersey Eq. 440 (1894) it was held that an attempt of the majority of stockholders to abrogate cumulative voting was a deprivation of a vested right and therefore illegal; while in New York's Appellate Division, First Department, *In the Matter of Jamaica Consumers Ice Co.,* 190 App. Div. 739, p. 741 (1920), unanimously affirmed, 229 N. Y. 516, held:

> "In Tomlin v. Farmers & Merchants Bank (52 Mo. App. 430, 436), the court said, referring to cumulative voting: 'The right is one guaranteed by law, constitutional and statutory; it is personal to the stockholder; it can be exercised or not by such stockholder as he may himself elect. (Pierce v. Commonwealth, 104 Pa. At. 155.) It, therefore, cannot be taken away from him by a resolution or by-law adopted by a majority of shareholders. (See, also, Attorney General v. Looker, 111 Mich. 498 *affirmed 178 U. S. 46;* Schmidt v. Mitchell, 101 Ky. 570.)" *Note: italic matter added.*

(c) When created pursuant to a Plan of Reorganization, approved by decree of the United States District Court, Cumulative and other Voting rights can be abrogated only in the manner provided in the Plan of Reorganization, and with the consent of the Bankruptcy Court which issued the decree approving the Plan. It is a judgment *in rem.* It may not be collaterally attacked or modified by a State Court, but effect must be given to it under the doctrine of *res judicata.*

Prudence Bonds Corp. v. *City Bank Farmers Trust Co.,* 186 Fed. 2nd 525 (2nd Cir.);

Diversey Building Corp. v. *Metropolitan Trust Co.*, 141 Fed. 2nd 65 (7th Cir.);
In re Pittsburgh Terminal Coal Corp., 183 Fed. 2nd 520 (3rd Cir.);
Stoll v. *Gottlieb*, 305 U. S. 165;
Gratiot County State Bank v. *Johnson*, 249 U. S. 248.

In *Gratiot County State Bank* v. *Johnson, supra,* this Court said:

> "The adjudication is, for the purpose of administering the debtor's property, conclusive upon the world * * *. So far as it declares the status of the debtor, even strangers to the decree may not attack it collaterally * * *. But an adjudication in bankruptcy like other judgments *in rem* is not *res adjudicata* as to the facts or as to the subsidiary questions of law on which it is based, *except as to parties to the proceeding or privies thereto.*"

In *Stoll* v. *Gottlieb, supra,* this Court had before it a Plan of Reorganization in 77 B Proceedings in Bankruptcy which had deprived a class of security holder of certain rights, which, despite such deprivation the courts of the State of Illinois had enforced as if unmodified by the Plan of Reorganization. Justice Reed, writing for this Court said:

> "This certiorari was allowed to review a judgment of the Supreme Court of Illinois. That court had denied effect to a plea of *res judicata* arising from orders of a district court in bankruptcy. Provisions declaring the supremacy of the Constitution and the extent of the judicial power and authorizing necessary and proper legislation to make the grants effective confer jurisdiction upon this Court to determine the effect to be given decrees of a court of the United States in state courts. As the contention is that the ruling

below disregarded decrees of a court of the United States it raised a federal question reviewable under Section 237 (b) of the Judicial Code, 28 U.S.C.A., Section 344 (b).

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"The Congress enacted, as one of the earlier statutes, provisions for giving effect to the judicial proceedings of the courts. This has long had its present form. This statute is broader than the authority granted by Article Four, Section One, of the Constitution to prescribe the manner of proof and the effect of the judicial proceedings of states. Under it the judgments and decrees of the federal courts in a state are declared to have the same dignity in the courts of that state as those of its own courts in a like case and under similar circumstances. But where the judgment or decree of the federal court determines a right under a federal statute, that decision is final until reversed in an appellate court or modified or set aside in the court of its rendition. *As this plea was based upon an adjudication under the reorganization provisions of the Bankruptcy Act, effect as res judicata is to be given the federal order, if it is concluded it was an effective judgment in the court of its rendition. The problem before the Supreme Court of Illinois was not one of full faith and credit but of res judicata. In this particular case, a federal question was involved. This was the power of the federal courts to protect those who came before them relying upon constitutional rights or rights given, as in this case, through a statute enacted pursuant to constitutional grant of power.*" (Italics ours.)

What has the Respondents' answer been to the applicability of *Stoll* v. *Gottlieb* in this Court? It will be found at the bottom of page 26 of the Respondents' Brief:

> "No one has challenged *Stoll* v. *Gottlieb*. It has no more application to this case than the Rule in Shelley's case.
>
> These alleged Federal questions simply do not exist. As Pooh-Bah remarked on another occasion, this 'is merely corroborative detail, intended to give artistic verisimilitude to an otherwise bald and unconvincing narrative.' "

Thus do Respondents seek with ridicule, banter and evasion to dispose of valid legal arguments they cannot squarely meet. If *Stoll* v. *Gottlieb* has no application to this case, it can have no validity as a precedent in any State Court, and the supremacy of the Federal Courts in bankruptcy reorganizations is at an end.

The Gilbert and Sullivan note aside, Respondents' sole and entire answer to the doctrine established by this Court in *Stoll* v. *Gottlieb, supra,* is to repeat the dictum of Judge McGohey "This reorganized debtor was in 1935 sent 'out into the state as fully subject to state law as though this court had nothing to do with its creation. In re Ambassador Hotel Corp., 2 Cir., 124 Fed. 2nd 435' " (Resp. Br., p. 21).

On February 1, 1951, however, the Circuit Court of Appeals for the Second Circuit overruled its decision of *In re Ambassador Hotel Corp.* See *Prudence Bonds Corp.* v. *City Bank Farmers Trust Co.,* 186 Fed. 2d 525, where it will be found that the Second Circuit has adopted the rule of the Seventh Circuit, in *Diversey Building Corp.* v. *Metropolitan Trust Co.,* 141 Fed. 2nd 65. Chief Judge Learned Hand, writing for the unanimous Second Circuit said:

> "* * * there has undoubtedly been considerable difference of opinion about the court's power to accommodate the original 'plan' to changes after confirmation in the financial situation of the 'revived debtor.' On this question we declared ourselves four times between

1942 and 1946. In In re Ambassador Hotel Corporation (124 Fed., 2d, 435) the State of New York had passed the 'Streit Law' affecting voting trusts after a 'plan' had been confirmed which set up a voting trust, whose duration, though lawful at the time, it was alleged that that act had cut down. We held that the state courts alone had jurisdiction to decide whether it had done so, and we did not mention the circumstance that the order of confirmation contained no reservation of powers, so far as appears. * * *

* * * We therefore conclude that our earlier decisions, in so far as they depended upon the presence of an express reservation in either the 'plan' or the order of confirmation, were erroneous.

The question is one of discretion, though of a discretion which should be sparingly exercised, and which should not be exercised as in North American Car Corporation v. Peerless Machine Corporation (143 Fed., 2d, 938, C. A. 3), unless the circumstances peremptorily demand it. * * * *The Court may never under the guise of 'alteration' or 'modification' substitute an entirely new plan in place of the original''*; citing *Diversey Building Corp.* v. *Metropolitan Trust Co.*, 7th Cir., 141 Fed. 2nd 65. (Italics ours.)

The rights of cumulative voting were assuredly vested property rights the source of which was the Plan of Readjustment in Bankruptcy. In no event could they be altered without the consent of a majority of the common stockholders and of the Bankruptcy Court. Petitioner went to great pains on the trial to prove that no order of the Bankruptcy Court was ever obtained authorizing the impairment of the cumulative and other voting rights. We are thus presented with a situation where the Courts of the State of New York have permitted the "alteration" and "modification" of the Hoe Plan of Readjustment. Two Circuit Courts of Appeals are agreed that this may not be done. Thus in *Diversey Building Corp.* v. *Metro-*

politan Trust Co., supra, Judge Sparks, writing for the unanimous Seventh Circuit said:

> "We cannot accept appellant's interpretation of sub-section (f) of this Act. We are convinced that Congress did not intend that a debtor-corporation should be permitted to ask for a radical change of plan of reorganization after it had been confirmed by the Court and was being executed under the Court's supervision. It is quite true that the quoted language from sub-section (f) states that changes and modifications may be proposed before or after a plan is confirmed; however, this sub-section must be construed with other pertinent sub-sections, such as (g) and (h), in determining the intention of Congress. *Here the plan as confirmed had been in operation for almost eight years, without complaint so far as this record shows, and it was originally proposed by the debtor itself. Under these circumstances we think the Court was without jurisdiction to entertain appellant's motion. We interpret sub-section (f) to mean that changes and modifications after the plan is confirmed refer to such changes as will better aid in carrying out the plan which has been finally confirmed, and not such changes or modifications as will materially alter the property rights established by the decree of confirmation, and in no event shall any change be made without the consent of the Court."* (Italics ours.)

Respondents conceded on the trial that no order of the Bankruptcy Court was ever obtained modifying the 1935 Plan of readjustment which gave the common stockholders the right to vote cumulatively and prohibited amendment of the corporate charter affecting their voting rights without the consent of a majority of the common stockholders.

Vandiver Brown, an "A" director of Hoe, secretary and general attorney for Johns-Manville Corporation and chairman of the special committee of directors, appointed

to consider the 1950 Plan of Consolidation, testified (R. 307):

"Q. What, if any, corporate necessity was there for accomplishing this consolidation, in your opinion?

* * *

The Witness: To eliminate cumulative voting.

Q. *Did you know on June 14, 1950, when you voted for the plan of consolidation, Plaintiff's Exhibit 8 in evidence, that it was the purpose and intention of the A directors to deprive the common stockholders of the right to vote cumulatively for the election of two directors?* A. *I did not, because it was not a fact; I did not know that because it was not a fact.*

Q. *I call your attention to paragraph 10th—* A. To *deprive them of the right to vote cumulatively?*

Q. *That's right.* A. *I knew that; I'm sorry, I answered too quickly. That was part of the plan, an important feature of it.*

The Court: *That was part of the plan?*

The Witness: *Yes"* (R. 315).

"Q. *Do you, or to your knowledge, did any of the defendants obtain an order from the United States District Court in any way or any manner modifying the order of March 1, 1935?*

The Court: *It is conceded that they did not.*

Mr. Cullom: *Yes, sir, but it is an incompetent question.*

The Court: *Let us have the fact to save time. It is conceded that they did not?*

Mr. Cullom: *Yes, sir.*

The Court: *There is no further order of Judge Coxe in this proceeding other than the one in evidence here.*

Mr. Cullom: *Because none was required.*

The Court: *Never mind the 'because,' I will take the fact; there was not any?"* (R. 316).

POINT III

Consolidation of two corporations under State law may not be availed of as a device to evade the provisions of a plan of reorganization in bankruptcy.

In the case of *Northern Securities Company* v. *United States,* 193 U. S. 197, two railroad companies, operating competitive lines, formed a third corporation into which both were merged under the laws of the State of New Jersey. The government brought suit to declare the merger invalid as a violation of the Sherman Anti Trust Law. The defendant Northern Securities Company contended that it was validly organized under the Laws of the State of New Jersey and that since what was done by it was legal in the State of New Jersey, it was necessarily legal in the Federal Courts. This court rejected the pious pretentions of the defendants; Justice Harlan, in the course of the majority opinion said:

> "Every corporation created by a State is necessarily subject to the Supreme Law of the Land * * * no device in evasion of its provisions however skillfully such may have been contrived, * * * is beyond the reach of the Supreme Law of the Land. * * * No Corporate person can excuse a departure or violation of that rule under the plea that that which it has done or omitted to do is permitted or not forbidden by the State under whose authority it came into existence" (193 U. S. 197, pp. 345, 347).

A comparable situation arose in *Tomlinson* v. *Branch,* 15 Wall. 460, p. 464, where Justice Bradley writing for this Court said:

> "In declaring that one company shall be merged in the other, and that the rights, privileges and property of the one shall be vested in the other, the legislature

> cannot be understood to mean that the restrictions, limitations and burdens affecting that property and imposed for the benefit of the public or of individuals shall not go with it. The rights and privileges go with it, and those rights and privileges can with difficulty be separated from the restrictions and duties by which they are measured and qualified."

Writing in the University of Pennsylvania Law Review in 1927, E. Merrick Dodd Jr. said (75, U. of Pa. L. Rev. 585, 736):

> "Where the Consolidated corporations are not engaged in public service * * *. The power of eminent domain probably does not extend to such a case, and the consolidation act must, therefore, depend for its validity on the reserved power to amend. Although this power is in terms unlimited, it does not authorize amendments which are inconsistent with the object of the original charter nor those which impair rights that have vested thereunder."

The *ratio decidendi* of the New York Court of Appeals in the case of *Beloff* v. *Consolidated Edison Co.*, 300 N. Y. 11, cited by the trial court was, that consolidation of two utilities was in the public interest. The Legislature of the State of New York (not the state judiciary as in the present case) had by virtue of its power of eminent domain, enacted a law permitting the merger of two public utilities on consent of the Public Service Commission of the State of New York where one company owned more than 95% of the shares of the other. The Court of Appeals held that where the public welfare was to be served by a merger effected pursuant to the enactment, a dissenting minority stockholder had to yield up his vested rights, and that he bought his shares subject to the power of the legislature to alter such rights. In the *Beloff* case, the dissenter was offered $135 per share at the time of the merger, which he could take without litigation if he chose not to take the

new shares offered him. Were it not for the fact that a public purpose was to be served by the merger, it is clear from the decision of this Court in *Treigle* v. *Acme Homestead Assn.* (1936), 297 U. S. 189, that the merger in the *Beloff* case would have been illegal. This Court said at page 196:

> "The statute merely attempts for no discernible public purpose, the abrogation of contracts between members of the association, lawful when made. This cannot be done under the guise of amending the charter powers of the corporation."

In the instant case, the public welfare of the State of New York is not involved. No public purpose is to be served. No legislative action has intervened. On the contrary, a self-seeking group of "A" stockholders, bent on defeating the Hoe Plan of Readjustment in Bankruptcy, which was approved by the solemn decree of the United States District Court, has succeeding in destroying the cumulative voting rights of the common stockholders and their ultimate right to take over the corporate control as outlined in the Plan. These vested rights of the common stockholders have been taken away under a masquerade of consolidation of Hoe, with a phantom called Hoe Export Import Corporation, a mere piece of paper, purchased at an expenditure of $50. This Court should not permit such a transparent and tawdry device to defeat the supreme law of the land.

That consolidation was adopted as a device to evade the provisions of the Plan of Readjustment so as to deprive the common stockholders of cumulative and other voting rights without their consent, appears conclusively from the following excerpts from the Minutes of the Directors Meeting held on June 28, 1950, fully two weeks before Hoe Export Import Corporation was organized at a cost of $50 by its chairman of the Board of Directors and General Counsel Cullom.

> "The Chairman then stated that he felt that existing conditions made it advisable for him to invite con-

sideration of a possible plan of re-capitalization. • • • *Mr. Cullom stated that he came to the conclusion that re-capitalization was not feasible on a basis of voluntary consent of all three classes of stock*" (R. 527).

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"Mr. Cullom stated that thirty or more plans had been examined in recent months and that certain groups representing the common stock had been particularly vocal in this connection" (R. 528).

"Mr. Cullom then proceeded to a discussion of the evil effects upon the Company of cumulative voting" (R. 529).

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"He then stated that, in view of the impossibility of obtaining the consent of two-thirds of the Common stock on a plan of recapitalization which would meet the approval of the A, he suggested that a consolidation with another corporation, perhaps a wholly-owned subsidiary, be effected, pursuant to Section 86 of the N. Y. Stock Corporation Law. He read to the meeting excerpts from Section 5-K of the certificate of incorporation, as amended, directing attention to the provision thereof to the effect that all voting rights were vested in the A stock (except to elect two directors and vote on dissolution) and that the Common stock was 'specifically excluded' from voting upon 'consolidation pursuant to Section 86 of the Stock Corporation Law.' In the opinion of counsel, neither Common nor B would have the right to vote upon such a consolidation" (R. 532).

In stating his concept of "The Issue" before this Court Respondents' Counsel Cullom asserts:

"The entire case therefore comes down to this simple proposition: Petitioner contends that there are two permissible alternatives, i. e., recapitalization through

consolidation under section 86; or by amendment under section 35 (the common stock had renounced its right to vote on either); and that the defendants chose the former rather than the latter which petitioner prefers; *ergo* fraud."

This is a wholly misleading statement of the issue.

FIRST: Former section 36 of the Stock Corporation Law was repealed by Laws of New York 1949 c. 805, sec. 1, effective Sept. 1, 1949; and, effective on that same date, sec. 10, c. 805, Laws of New York 1949, added a new Section 35 to the Stock Corporation Law, and provided in an amended Section 51 thereof, "that the holders of all outstanding shares whose rights will * * * be adversely affected by such action (*i. e.* reclassification under Section 35) shall be entitled to vote, * * * in either event *regardless of any provision to the contrary in the certificate of incorporation or other certificate filed pursuant to law.*" (Italics added.) Hence, one of the two so-called alternatives was not permissible without the consent of the common stockholders, which Mr. Cullom had previously told the Board was impossible to obtain (R. 532).

SECOND: With regard to the other so-called permissible alternative, the correct statement of Petitioner's contention is as follows:

On June 25, 1935, the United States District Court ORDERED, ADJUDGED AND DECREED * * *(R. 444-462)

"5. By orders dated May 15, 1935, June 5, 1935, and June 10, 1935, made, and entered, after hearings duly adjourned, and by an order of the Court of even date herewith, the Court has approved the following documents for the consummation of the Plan after finding that such documents had been prepared by counsel for the Debtor and duly approved by the Board of Direc-

tors or the Committee of the Board of Directors as required by the Plan:

* * *

(b) Certificate of increase of number of shares, of change of all its previously authorized shares without par value, issued and unissued, into the same number of shares with par value of classification of shares, with par value, and of change of the statement respecting its capital contained in the Certificate of Incorporation of the Debtor;

(c) Certificate of increase of number of directors:"

The foregoing Decree of the Federal Court, approving the amended Certificate of Incorporation, merely carried out the Plan of Readjustment; and the right of the Debtor to consolidate under Section 86 without the common stockholders' approval—upon which Respondents base their entire defense—was contained in the very same Plan of Readjustment and Certificate of Change and Increase which unequivocally established the right of cumulative voting, and which provided that the common stockholders' rights to vote cumulatively for directors, could not be impaired without their majority consent. (These rights are now characterized by Respondents as immaterial exceptions.) Petitioner therefore contends that resort cannot lawfully be had to a consolidation under section 86 of the Stock Corporation Law to evade the provisions of the Plan of Readjustment and that such "consolidation," depriving the common stockholders of their cumulative and other voting rights, could not be accomplished without the consent of the majority of the Common stockholders and the approval of the Federal District Court, first obtained on notice.

POINT IV

The Federal questions were saved for review by presentation at the trial court, at the Appellate Division and at the Court of Appeals of the State of New York. Petitioner is prepared to accept Respondents' summary of the Federal question as it appears in the respondents' briefs below, as a basis for the granting of a writ by this Court.

Respondents urge as ground for the denial of the Writ of Certiorari, that "No certificate has been obtained from the highest state court to the effect that a Federal question was raised and decided. The decision passed on non-Federal grounds" (Resp. Br., p. 27). Petitioner annexes to the appendix a letter from Raymond J. Cannon, Clerk of the Court of Appeals, stating that such is not the practice of the Court of Appeals, and that it is its practice to certify the motion papers for leave to appeal and any opposition papers. Accordingly petitioner has obtained certified copies of the briefs and moving papers of both parties at the Court of Appeals and at the Appellate Division, which are to be filed with the Court simultaneously with this Brief. Pertinent extracts from these papers are printed in the appendix. They show that the Federal questions were at all times before the State Courts and consequently are saved for review by this Court.

In order however to avoid a prolix discussion on the subject in this Reply Brief, Petitioner is prepared to accept, with slight modification Respondents' own summary of Petitioner's presentation of the Federal question appearing at p. 62 of the Respondents' Brief at the Appellate Division and page 58 of the Respondents' Brief at the Court of Appeals. In both of these State Courts, identical language was used by Respondents' Counsel to describe the Federal Question presented by Petitioner in every court before which Petitioner has appeared. It is as follows:

"In his brief Katz urges that this consolidation violates the plan of reorganization approved by the Federal Court in the Hoe 77 B proceeding of 1935—or, to state it differently, that the certificate of incorporation, as amended and approved by that court when the debtor was discharged in 1935, immutably defines the rights of the stockholders; and cannot later be amended or altered in any respect or by any means."

Petitioner suggests the following modification of Respondents' summary of his presentation of the Federal Question as the basis for the issuance of the Writ of Certiorari herein.

The Federal Questions presented (as amended): Whether the consolidation of Hoe with its subsidiary violates its Plan of Readjustment and Amended Certificate of Incorporation both approved by the Decree of the United States District Court in the 77 B Proceeding of 1935, by depriving the common stockholders of their vested cumulative and other voting rights without their majority consent, and without the approval of the United States District Court, both of which are immutably required by said Plan and by the Decree of the U. S. District Court approving it?

POINT V

Since the constitutional question was not the sole question presented to the New York Court of Appeals for its consideration Petitioner was not entitled to appeal to that court as a matter of right and the denial by it—the highest court of appellate jurisdiction of the State of New York—of Petitioner's motion for leave to appeal requires that the Writ of Certiorari issue to the Appellate Division, the intermediate appellate court which rendered the final judgment herein.

In the case of *Lewis* v. *Board of Education*, 275 N. Y. 481 the Court of Appeals of the State of New York dismissed an appeal, assertedly taken by the appellant as of

right, under the provisions of section 588 of the New York Civil Practice Act, because there was "directly involved the construction of the constitution of the state or of the United States." The "Appeal (was) dismissed with costs, on the ground that the constitutional question is not the sole question involved in the appeal."

A mere examination of the papers submitted by both parties at the Court of Appeals shows that more was involved in the appeal to the Court of Appeals than a constitutional question. Indeed, Respondents urge such State grounds of decision as a basis for the denial of this petition. To be appealable to the Court of Appeals as of right, the judgment must have been addressed exclusively to a constitutional question, under the State or Federal Constitutions. Such is the clear holding of the Court of Appeals in *Lewis* v. *Board of Education, supra.*

In *Southern Electric Co.* v. *Beha,* 269 U. S. 186, cited by Respondents at pages 15-17 of their brief, this Court, by Taft, Ch. J., held that a Writ of Certiorari did not lie to this Court where "no application was made for leave to appeal to the Court of Appeals" (p. 189). This all-important statement is omitted from the passage of Chief Justice Taft's opinion quoted at page 16 of the Respondents' Brief.

Since under the decisions of the Court of Appeals of the State of New York, application for leave to appeal was necessary, and since Petitioner made such application without success, the denial by the Court of Appeals of Petitioner's motion for leave to appeal clearly leaves the Appellate Division, First Department, as the state court to which the Writ of Certiorari should issue herein. *American Railway Express Co.* v. *Levee,* 263 U. S. 19.

POINT VI

Federal Judge McGohey ruled on November 6, 1951, "the petitioner sought and failed to justify the intervention of the State Court. He cannot, while pressing his appeal there, relitigate the same issues in this Court. (*Davega City Radio Inc.* v. *Boland*, D. C. S. D. N. Y., 23 F. Supp. 969, 970.)" His decision dismissing the Petitioner's application for relief in the Federal Courts is therefore not *res judicata* in the very appellate courts to which Petitioner appealed, pursuant to the suggestion of Judge McGohey, nor in this Court, where the State Court judgments are sought to be reviewed.

Respondents' counsel in the brief submitted in opposition to this application has tried to make a game of "Catch the Fox" out of this litigation. In his affidavit submitted in opposition to the motion for injunction *pendente lite* the said Neil P. Cullom swore "If, therefore, plaintiff has any quarrel with the restrictions upon the Common Stock's right to vote, it is with the Federal Court and not with this management" (see appendix).

When Petitioner, following the suggestion contained in Mr. Cullom's affidavit, applied to the Federal Court for an injunction to restrain the violation of the Federal Court decrees in the Bankruptcy Proceeding, Mr. Cullom not only endeavored to punish the Petitioner and his Attorney for contempt of Court (see affidavit annexed to petition), but he also contended that the appeal to the State Appellate Courts was the exclusive remedy of the petitioner.

Judge McGohey on November 8, 1950 dismissed the Petitioner's application for an injunction and relegated the Petitioner to his appeal to the State Courts. His opinion quoted in the headnote makes that clear. Petitioner therefore filed his appeal to the Appellate Division on November 16, 1950 (R. 5-6).

Petitioner attempted to appeal to the Circuit Court of Appeals for the Second Circuit thereafter, but that court dismissed his appeal. It would not amend its order of dismissal on petition for rehearing, so as to make clear the ground of its dismissal. In the affidavit annexed to this brief as an appendix, it is shown that because the Circuit Court of Appeals refused to clarify the basis of its decision, a petition for a Writ of Certiorari did not lie to this Court from the Circuit Court's order of dismissal.

In every court to which the Petitioner has applied for relief, the Respondents have urged that Petitioner belonged in another court. When he has arrived at that court it has been urged that the adjudication of another court bars relief. In the Federal Court before Judge McGohey it was asserted that the decision of Judge Cohalan barred relief before Judge McGohey. The only avenue of redress it was claimed was by appeal to the State Appellate Courts. Judge McGohey relegated Petitioner to his appeal to the State Courts. Now it is asserted that this Court is bound by the decision of Judge McGohey as *res judicata.* The law is not a game of "Catch the Fox." It is submitted that when the fox is at last at bay, he should be compelled to meet the issue and not be permitted to escape on any trumped-up issue of *res judicata.*

While it is true that Judge McGohey asserted as an additional basis for relegating Petitioner to his remedy by way of appeal to the State Court's that "this reorganized debtor was in 1935 sent out into the state as fully subject to state law as though the court had had nothing to do with its creation" citing *In re Ambassador Hotel Corp.* v. *Peerless W. & V. Mach. Corp.,* 2 Cir., 143 F. 2nd 938, the foregoing citation was dictum and was overruled by the Second Circuit in *Prudence Bonds Corp.* v. *City Bank Farmers Trust Co.,* 186 Fed. 2nd 525, decided February 1, 1951.

POINT VII

The non Federal grounds assigned by the State Courts as a basis for decision are not adequate to defeat review by this Court. The failure or refusal of the State Courts to pass upon the Federal issues, which would have been and are decisive of the entire litigation, "may be properly regarded as essentially arbitrary, or a mere device to prevent a review of the decision upon the Federal question".

Enterprise Irrig. Dist. v. *Farmer's Mutual Canal Co.*, 243 U. S. 157;
Lawrence v. *State Commission*, 286 U. S. 276, page 282.

The Trial Court fully understood that the 1935 Plan of Readjustment in Bankruptcy was controlling on everyone and on Petitioner's cumulative voting rights as of the date of the trial in October 1950. Nevertheless the Trial Court failed and refused to pass upon the Federal issues.

At Record page 282 Mr. Cullom, Respondent's counsel and author of the 1950 Plan of consolidation, offered in evidence an exhibit (Defendant Hoe's Exhibit AU). In ruling upon the admissibility of this document the Trial Court said (R. 283):

> "The Court: *I understood that the amendment, which was practically at my direction because I thought he had pleaded himself out of court without the amendment, was to the effect that the 1935 action of the Federal Court, and which had occurred here was controlling on everyone. I further understood you all agreed that that Federal matter was controlling. I don't see that I need take anything else.*"

By cross examination of Charles E. Littleton, Secretary of the Respondent Hoe, Petitioner proved that cumulative

voting by the Common stockholders came into effect in 1945 under the Plan of Readjustment in Bankruptcy, dated 1935 (R. 283-287). Ten full years had elapsed before it became effective.

"By Mr. Garfield (R. 283):

Q. Is it not a fact that the preferred stock, prior preferred stock referred to on page 22 and 23 of Plaintiff's Exhibit 1—I will show you this copy—

Mr. Cullom: *I think we can cover that by concession.*

The Court: *What is this?*

Mr. Cullom: *He asked me to concede that the prior preferred stock of this corporation was retired at various times up to the fiscal year of 1945* (R. 284).

The Court: Gentlemen, you both, apparently, want to go back into the past of this corporation. I don't think it is necessary and I think you are unduly prolonging this litigation. *I am confronted with a problem of deciding whether, on a certain day in the year 1950 when this new plan was adopted, anything illegal or unfair in the eyes of a court of equity to the common stockholders, was done. That is my only problem.* What was done that was illegal or praiseworthy on some other occasion is of no moment here.

Mr. Garfield: *My question is directed directly to that proposition.*

The Court: *To 1950?*

Mr. Garfield: *Yes, directly to this day, to this very minute.*

The Court: *All right, ask a new question.*

Q. *Has the prior referred stock been paid in full and liquidated?*

The Court: Answer, yes or no.

A. *At that time, yes.*

Q. *In 1946?* A. *Yes.*
Q. Since 1946—

The Court: *What has that got to do with how things existed in 1950?*

Mr. Garfield: *Because the plan provides, the plan of the United States District Court provides, that the second the prior preferred stock has been eliminated the common stockholders have the right to elect two directors, voting cumulatively.*

The Court: *In other words, by the order of reorganization in the United States District Court this becomes of moment in deciding conditions as they were in 1950; is that it?*

Mr. Garfield: *Exactly.*

The Court: *Then, I will take it. Is that right?*

Mr. Cullom: *Wasn't that 1945?*

The Witness: *The retirement, I think, was completed in 1945.*

Q. When did the A directors, for the first time, elect nine directors? A. I have a date in mind, but it was shortly before that retirement.

Q. *You were in the employ of the defendant, R. Hoe & Co., Inc., during all of the time that it was in the 77-B proceeding, were you not?* A. *I was.*

Q. You were familiar with this plan of reorganization? A. I was.

Q. And were you familiar with the provisions of page 22, the first paragraph, paragraph 1, under the heading "Miscellaneous"? A. Yes.

Q. *And since the year 1946, have not the common stockholders elected two directors voting cumulatively?* A. *Yes.*"

The foregoing testimony, coupled with the concession that no order of the Bankruptcy Court was obtained modifying the Plan of Readjustment (R. 316) left the Trial Court with a single question of Federal law which would

have been determinative of the entire litigation, and which the Trial Justice himself had declared, during the trial, to be "controlling" (R. 283).

Neither the Trial Court nor the Appellate Division placed their decisions upon the Federal Questions raised by Petitioner's Second Amended Complaint, which are amply supported by the proof and concessions. Indeed that there was a studied evasion of the Federal Questions becomes apparent from an examination of the opinions rendered by both said Courts. It is to be borne in mind that the Appellate Division did not sustain every contention of the Trial Justice. It placed its decision on a concurrence with the Trial Court's finding that (1) there was no showing of fraud and (2) the balancing of equities required affirmance of the judgment. Let us however proceed upon the assumption erroneously advanced by Respondents, *i. e.*, that the Appellate Division adopted all of the findings of the Trial Justice. It will be found that the alleged state grounds of decision are not adequate to defeat the Federal questions which were duly raised in all the State Courts and which if decided, would have been dispositive of the case without touching upon any State question. In making this assertion we confine ourselves to the Amended Federal Question appearing at page 19 of this Reply Brief as follows.

THE FEDERAL QUESTION PRESENTED (as amended)

Whether the consolidation of Hoe with its subsidiary, violates its Plan of Readjustment and Amended Certificate of Incorporation both approved by the decree of the United States District Court in the 77B proceeding of 1935, by depriving the common stockholders of their vested cumulative and other voting rights without their majority consent, and without the approval of the United States District Court, both of which are immutably re-

quired by said Plan and by the decree of the United States District Court approving it?

Here then are the six non-Federal grounds of decision as summarized at page 22 of the Respondents' Brief:

> FIRST: That under the law of New York (Section 21, Stock Corporation Law) Plaintiffs have an adequate remedy at law in the form of appraisal;
>
> SECOND: There was no proof of fraud;
>
> THIRD: Under the terms of the company's charter, "The present common stockholders have no right to vote on the proposed consolidation";
>
> FOURTH: There was no "ruse" or subterfuge "by means of which the provisions of Section 35 was being avoided";
>
> FIFTH: There was a complete failure of proof as to any unfairness to the common stock;
>
> SIXTH: That it is settled law of this state that "in the absence of a very plain showing of either fraud or improvidence" the court "will not substitute its judgment for that of the directors or stockholders as to the economic wisdom of plans of this nature".

In considering the above grounds of State decision it is well to bear in mind this Court's repeated rulings that the Supreme Law of the land as embodied in the Constitution of the United States and statutory enactments pursuant thereto such as the Anti-trust and Bankruptcy laws must prevail over State laws regulating corporate affairs and conduct.

> *Northern Securities Company* v. *United States,* 193 U. S. 197;
> *Stoll* v. *Gottlieb,* 305 U. S. 165;
> *Voeller* v. *Neilston Warehouse Co.,* 311 U. S. 531, 535.

Nothing in the cases cited by Respondents in Point III of their brief detracts one iota from this principle. Thus in *Wood* v. *Chesborough,* 228 U. S. 672, the non-Federal grounds of decision were the doctrine of laches and the State Statute of limitations which were adequate, in and of themselves to support the State Court decision.

This Court said in *Wood* v. *Chesborough, supra,* at page 677, immediately following the portion of its decision quoted at page 24 of Respondents' Brief.

> "* * * *the sufficiency of the Federal right set up cannot be evaded if necessary to the determination of the case, and, it may be admitted, that of such necessity this court must in each instance decide* (citing cases). In Cresswill v. Grand Lodge K. P. 225 U. S. 246 it is decided that this court will review the findings of fact by a state court (a) where the Federal right was denied as a result of them and there is no evidence to support them, a question of law hence resulting for decision; and (b) where a conclusion of law as to a Federal right and finding of fact are so intermingled as to cause it to be necessary, for the purpose of passing on the Federal question, to analyze and dissect the facts. To the extent necessary to do so the power exists as a necessary incident to a decision upon the claim of denial of the Federal right." (Italics ours.)

In *Fox Film Corporation* v. *Muller,* 296 U. S. 207, the following significant quotation explanatory of this Court's decision in that case, was omitted from Respondents' Brief (p. 23):

> "Whether the provisions of a contract are non-severable so that if one be held invalid the other must fall with it is clearly a question of general and not Federal law * * *. It follows that the non-Federal ground is adequate to sustain the judgment.

> The rule announced in Enterprise Irrig. Dist. v. Farmers Mutual Canal Co., 243 U. S. 157 and other cases, to the effect that our jurisdiction attaches where the non-Federal ground is so interwoven with the other as not to be independent matters, does not apply."

An analysis of *Wall* v. *Parrott Silver & Copper Co.*, 244 U. S. 407, cited by Respondents at 24 of their Brief clearly shows the shallow nature of Respondents' argument. Justice Clarke's opinion indicates that two distinct questions were there presented, one cognizable under State law and the other Federal. Each was independent of the other. They were:

(1) Was there a fraudulent dissipation and depreciation of assets to the detriment of a minority stockholder for which he had a cause of action under Montana law?

(2) Was the Montana Statute, which required the minority stockholder to take on appraisal the value of his shares at the date of appraisal, without giving effect to the value of property fraudulently dissipated, a deprivation of the Petitioner's property in violation of the Fourteenth Amendment?

The dictum of this Court quoted at page 25 of the Respondents' Brief was not the basis of decision, for immediately following the quoted statement, this Court said:

> "We prefer not to have the case go off on this rule * * *. This record does not call upon us to examine into this challenge * * * for the reason that the appellants, by their action in initiating a proceeding for the valuation of their stock, pursuant to these statutes, which is still pending, waived their right to assail the validity of them."

This brings us directly to the First ground of non-federal decision of the trial Court *i. e.* "That under the laws of New York (Section 21 of the Stock Corporation Law) plaintiffs have an adequate remedy at law in the form of appraisal." This contention is directly the opposite of the reason for dismissal of the writ by this Court in *Wall* v. *Parrott Siver & Copper Co., supra.* Petitioner did not file for appraisal, nor did he take a single step inconsistent with his contention that the Consolidation was void under the Plan of Readjustment in Bankruptcy and that it therefore offended the Supreme Law of the land.

In the case of *Breslav* v. *N. Y. & Queens Elec. Light & Power Co.*, 249 App. Div. 190 (unanimously affirmed, 273 N. Y. 593), the Appellate Division, Second Department, said with respect to a similar contention:

> "The remedy of appraisal under section 38, which the learned Special Term said was available to plaintiff, applies only if the amendment alters the preferential rights of outstanding shares. *As heretofore indicated, the proposed amendment* does not alter any preferential rights running with the shares but *destroys a vested property right. Defendants admit the remedy of appraisal is not an adequate or even an available remedy if the proposed change is not authorized.* * * *
> * * * this reserved power (to alter corporate charters) is not unlimited, and its exercise is subject to the restrictions and restraints by the other provisions of the State and Federal Constitutions. Due process of law must be observed and vested property rights and obligations of contracts must not be destroyed or impaired. (Coombes v. Getz, 285 U. S. 434; Philips Petroleum Co. v. Jenkins, 297 U. S. 629.)"

It is to be noted that although the Respondents urged at the Appellate Division that "Appellants have an adequate remedy at law: appraisal constitutes the exclusive

remedy of a stockholder not wishing to participate in the plan", that the Appellate Division did not accept this argument as a basis for decision. Instead, it adopted the Trial Court's finding that there was no fraud.

The remaining five grounds of decision of the Trial Court and the grounds of decision by the Appellate Division have been fully covered in the Petition. They may all be linked in one category, namely that there was no fraud shown. The Certified copies of the Petitioner's and Respondents' Briefs at the Appellate Division which are submitted herewith, show that the Federal Questions would have been conclusive over all the alleged non-federal questions. Petitioner urged *at both* the Appellate Division and the Court of Appeals.

> **That "the real purpose for the organization of Hoe Export-Import Corporation was to use it as a fraudulent device to deprive the common stockholders of Hoe of their right to take over the ultimate control of Hoe from the 'A' stockholders, under the provisions of the Plan of Readjustment in Bankruptcy, without affording the common stockholder the right to vote thereon. The Federal Court's decrees being judgments *in rem* are *res judicata* and are binding on all Courts, parties and their privies."**

Respondents' answer to the foregoing point has been the same at both the Appellate Division and at the Court of Appeals. Indeed the almost identical language was employed in both courts, *i. e.*

"POINT VII

THERE HAS BEEN NO VIOLATION OF THE FEDERAL COURT ORDERS.

In his brief Katz argues that this consolidation violates the plan of reorganization approved by the Federal Court in the Hoe 77 B proceeding of 1935—or, to state it differently, that the certificate of incorporation,

as amended and approved by that court when the debtor was discharged in 1935, immutably defines the rights of the stockholders; and cannot later be amended or altered in any respect or by any means. To state the claim is to answer it.

Both lower courts and the Federal courts, have dismissed the contention as unsound;"

It is respectfully submitted that no state court has passed upon the above Federal question, let alone dismissed it as unsound. And as for Judge McGohey's decision, as previously shown, he merely relegated the petitioner to his appeal to the State Courts. Everything else that he said was mere *dictum.*

The evasion of the Federal questions by the State courts being fully shown, since the said questions would have been determinative of the controversy, the alleged non-federal grounds of decision do not bar a review by this court.

Conclusion

Respondents' Counsel, Neil P. Cullom, author of the 1950 Plan of Consolidation, in order to avoid answering before this Court for his studied violation of the 1935 Federal Court decrees and the impairment of the vested rights of the common stockholders, resorts to a vicious *argumentum ad hominem,* and an attack upon the honor of Petitioner and his counsel: He has falsely insinuated that Petitioner's Counsel has filed the petition herein without the knowledge of petitioner (R. Br., p. 13); falsely insinuated that petitioner is not "now a *bona fide* beneficial, owner of Hoe stock" (R. Br., 14) and falsely accused petitioner's counsel of "manufacturing out of the whole cloth a quotation from Wormser on the Disregard of the Corporate Fiction" (p. 18). (See pages 13 and 14 Respts. Br.)

A measure of the man responsible for this intemperate language may be gathered from what the Appellate Divi-

sion, First Department said of him in October, 1922, in the case of *Pelzer* v. *Perry,* 203 App. Div. 58, 60, in which case the same individual, Neil P. Cullom, was counsel for the Respondent. Justice Page, writing for the unanimous bench, said:

> "We regret to note that counsel for the respondent in each of the four briefs which he has filed on the various appeals in this case has adverted to a matter that formed no part of the record on these appeals, and used intemperate and impertinent language intended to reflect upon one of the justices. Because of this matter being in the briefs, the four briefs will be ordered stricken from the files, and the counsel is admonished that a repetition of the offense will call for more drastic action."

Anyone looking at the quoted matter on page 18 of the Petition can see that it is an extract from Petitioner's briefs below. It was not claimed to be nor is it a quotation from Wormser, although Wormser is cited as authority for the point urged. What Wormser actually did say is so much more potent than anything said by Petitioner, that it is well to conclude this brief with Wormser's actual words.

> "Oftentimes the corporate form of organization is adopted in an endeavor to evade a statute or modify an intent. A forceful example is to be found in the learned decision of the United States Supreme Court disregarding the theory of corporate entity in enforcing the 'commodities clause' of the Hepburn Act. (*U. S.* v. *Lehigh Valley R. R. Co.* [1911], 220 U. S. 257, 31 Sup. Ct. 387 [per White, C. J.]). The commodities clause provides that:
>
> > "'It shall be unlawful for any railroad company to transport from any State * * * to any other State * * * any article * * * manufactured, mined or produced by it, or under its authority, or which it may own in whole or in part, or in which it may have any interest, direct or indirect * * *.'

"The government, in the first suit, alleged that the Lehigh Valley Railroad Company owned stock in a coal company whose goods it was carrying. On demurrer, it was held that no violation of the statute was thereby shown; the court interpreted 'interest, direct or indirect' as meaning only a legal or equitable interest in the transported articles. (*U. S.* v. *Delaware & Hudson Co.* [1909], 213 U. S. 366, esp. 413.) The government, after this first and very serious blow, presented an amended complaint in which it was set forth, in addition to the allegations of the prior complaint, that the railroad company was using the coal company merely as a sham, a device and a dummy, in order to evade the provisions of the act.

"The court held that no such evasion could succeed, and, disregarding the corporate concept and looking at the substance and reality of things, decided that it was within its jurisdiction to issue an injunction. (1911, 220 U. S. 257 *et seq.*) It is submitted that every dictate of sound reason warranted the court in holding as it did.

"The late Justice Brewer in his notable concurring opinion in *Northern Securities Company* v. *United States* (1903), 193 U. S. 197, 360-4, pointed out that, where a corporation, was organized merely as a convenient means of combining separate railroad properties under one control the court could shake aside the veil of entity and regard the combination as just 'as direct a restraint of trade by destroying competition as the appointment of a committee to regulate rates.' In other words, the plain intent and purport of the Sherman Anti-Trust Act cannot be defeated by a resort to the sham and subterfuge of incorporation."

* * *

"The burning words of a late Chancellor of New Jersey should be borne in mind by every corporation lawyer who seeks to use the concept of corporate

entity to defeat the end for which it was invented: (*Stockton* v. *Central R. R. Co.* (1892), 50 N. J. Eq. 52, 75-76, citing abundant authority.)

"'* * * A more flimsy device, when the particulars are once known, it is impossible to imagine. It may succeed for a time in baffling persons. * * *' It must not be thought that courts are powerless to strip off disguises that are designed to thwart the purposes of the law. The mere suggestion of such a condition is an insult to the intelligence of the judiciary. Whenever such disguises are made apparent, they can readily be disrobed. The difficulty is in showing the disguises, not in penetrating them when they appear.

"A recent decision, following numerous others, by the United States Supreme Court, speaking through the late Justice Harlan, emphasizes another phase of the disregard of the corporate entity where the corporation is a mere shift to evade the law. In that case, a corporation was formed for the sole purpose of attempting to get certain litigation into the federal courts and thus of invoking federal rather than state jurisdiction. The entity was impatiently, almost contemptuously, disregarded. (*Miller and Lux* v. *East Side Canal, etc., Company* (1908), 211 U. S. 293, and cases cited.)

"Further illustrations *ad infinitum* might be given: they would serve not so much further to fortify this principle as to introduce needless repetition."

Petitioner respectfully prays that his Petition for a Writ of Certiorari be granted.

Respectfully submitted,

GUSTAVE B. GARFIELD,
Attorney for the Petitioner.

Appendix.

Affidavit of Nathan Katz.

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1951

No. 360

NATHAN KATZ, individually and suing on behalf of himself and all other common stockholders of R. HOE & CO., INC., similarly situated,

Petitioner,

against

R. HOE & CO., INC., *et al.*,

Respondents.

STATE OF NEW YORK
COUNTY OF NEW YORK } ss.:

NATHAN KATZ, being duly sworn, deposes and says:

I am the Petitioner herein. Contrary to the insinuation appearing at pages 13 and 14 of Respondents' brief that the petition was filed by my attorney without my authority or knowledge, I solemnly state to this Court that the petition was filed with my full knowledge and authority and that I earnestly seek and pray that a Writ of Certiorari issue herein.

Respondents further assert at page 14 of their brief:

> "There is no evidence that petitioner even knows that this application is being made or that he is now a *bona fide* beneficial, owner of Hoe stock."

The fact is that I am now and since December 23, 1949, at all times have been a *bona fide* beneficial owner of 500 shares of the common stock of R. Hoe & Co., Inc.

The affidavit of Charles E. Littleton, secretary of Respondent Hoe, asserts that I bought my shares "at just about the time this plan was being considered." I solemnly declare that at the time I purchased these shares, purely as an investment, I had not the slightest knowledge of any contemplated plan of recapitalization or consolidation in any form whatsoever. Indeed, plaintiff's president, the Respondent Auer, addressed a letter to all stockholders on December 1, 1949, in which he said:

> "It has come to our attention that there have been rumors of an impending recapitalization. No recapitalization plan has been considered by our Board since the adoption of the plan placed in effect early in 1947."

A copy of this letter was sent to me by Mr. Auer immediately after I became a stockholder; late in December, 1949.

At a meeting of the Board of Directors of Respondent Hoe, held on May 24, 1950, it was

> "Resolved that the President be authorized to issue the following announcement:
>
> The Directors of the Company have approved no plan of re-capitalization and there is no immediate prospect of such approval" (R. 523).

The first and only knowledge that I obtained of the proposed plan of consolidation was a published statement which appeared in the New York daily press shortly after July 14, 1950. The first official notice I received of the proposed action was the company's proxy statement

(Plaintiff's Exhibit A, R. 482-3) which was mailed to me on or about August 8, 1950.

If any plan of consolidation or reclassification was being considered, I was not only without knowledge of that fact, but was misled to the contrary by the repeated assertions of Respondent Hoe's officers.

At page 35 of my petition, asserting the importance of the issues herein, it is stated

> "It is of tremendous importance to stockholders, large and small alike, that the rights of cumulative voting granted by contract to stockholders be protected by this court as a vested property right, so that stockholders like the holders of 93,000 common shares in this case will not again be compelled to risk a lawsuit to perserve their voting rights and thereby waive appraisal, doubtful as it may be as a remedy.
>
> "From the sheer monetary point of view, the petitioner and the holders of 93,000 common shares of Hoe have been deprived of property without compensation worth over $1,500,000. This is arrived at as follows:
>
> "Considering that there were 95,977 shares of A stock outstanding at the time of the consolidation and that two shares of new common stock (having a present market value of eight dollars per share), were issued without lawful right, for each A share outstanding, the amount unlawfully taken was $1,535,952. If it is impossible to unscramble the omelette, as ruled by the Appellate Division, the common stockholders are clearly entitled to an award of damages for such unlawful taking of their property."

Mr. Littleton culls one short passage from the foregoing statement (Respondents' Brief, p. 50) and asserts that it

is utterly false; but he presents nothing to controvert the accuracy of my above-quoted calculation. Instead, he asserts "there is not one stockholder who joins him in this effort to prolong this litigation and no one will have anything to do with this strike suit" (Respondents' Brief, page 50).

In this connection, I respectfully call the attention of this Court to the fact that when proof was offered upon the trial indicating "that neither the plaintiff nor, for that matter, the defendant Martin, stand alone," the Trial Court ruled as follows:

> "The Court: *I am not interested in that. If a man stands alone and still has rights, as far as I can, I will enforce those rights. My ruling is, I don't care about the number of people who may have taken a particular course at a particular time. If any one person is wronged, and that goes for your client and for the other plaintiffs here, by what was done, that is enough for me*" (R. 122-123).

That the record does not show the great number of common stockholders whose interests are being protected by this action, is entirely due to the Trial Court's ruling excluding such evidence.

This is not a strike suit. I have at all times since 1927 been a member in good standing of the Bar of the State of New York. Prior to the institution of this present suit, I have never commenced or participated in a stockholders' action, either as attorney or as party plaintiff. As I testified upon the trial of this action, no stockholder has paid or promised to pay my expenses for this litigation, either directly or indirectly (R. 68). I brought this action to protect my investment and to preserve my lawful property rights, and with no other motive whatsoever.

Appendix.

It is asserted by Respondents that this action is groundless and moot. This I deny. From the very outset of the litigation, I have prayed for a declaratory judgment declaring the proposed plan of consolidation unlawful, null and void under the Constitution of the United States. In my second amended complaint, served pursuant to the direction of the Trial Court, I prayed for

> "a declaratory judgment that the said proposed meeting, if it be held pending the trial of this action, is unlawful, null, void and of no effect in law, in violation of * * * the Constitution of the United States of America and Amendments 5 and 14 thereof, * * * and the plaintiff prays for such other alternative or different relief as may appear to be just and proper in the premises" (R. 15-16).

In my said second amended complaint, I alleged that the said "consolidation" was

> "in violation of the voting rights conferred upon the common stockholders as a class, by the decrees of the United States District Court for the Southern District of New York and the Plan of Reorganization therein set forth and incorporated dated March 1, 1935, and April 25, 1935, which decrees and Plan of Reorganization are heretofore referred to in paragraphs Second and Third hereof" (R. 14).

In paragraphs second and third of my second amended complaint, I set forth in detail the origin, history and nature of the class voting rights of the common stockholders including their right to vote upon any amendment of the certificate of incorporation which "shall be made which shall impair the right of the common stock voting as a class to elect and continue in office two members of the Board of Directors as such Board shall be constituted from time to time, or which shall impair the class voting

rights of the Common Stock on matters other than the election of directors conferred upon it by the foregoing provisions of this sentence'' (R. 9-11). My complaint then proceeds to allege in concrete detail how these rights are sought to be destroyed by Respondents' consolidation plan (R. 14).

The identical issues posed by my second amended complaint, litigated upon the trial, and briefed at the Appellate Division and at the Court of Appeals, have been presented to this Court as the Federal Question sought to be reviewed by this petition. It is a question that has never been directly presented to this Court, although closely related questions have been decided by this Court in *Stoll* v. *Gottlieb,* 305 U. S. 165, sustaining the position taken by me.

Every stockholder who purchased the newly issued shares has purchased them with constructive if not actual notice of *lis pendens.* He has purchased shares issued unlawfully to the A stockholders. Such new purchasers are not before this Court. The Respondent directors seek to prevent an accounting for the new common shares unlawfully taken by them, by hiding behind the so-called innocent purchasers of these newly-issued shares. Despite the consummation of Respondents' plan, made possible only by virtue of the Appellate Division's *vacatur* of the stay against such consummation, Petitioner respectfully maintains his right to a declaratory judgment that the plan was null and void and in violation of the 1935 Plan of Readjustment.

If, therefore, it be adjudicated that a legal and actionable wrong has been done to me, the Petitioner, it was a legal and actionable wrong to all the common stockholders, and the appeal should not fail because of mootness, despite the complexity of the situation brought about by the *vacatur* of the stay by the Appellate Division and the

consequent consummation of the plan. This Court may well find and decree that the plan of "consolidation" was void *ab. initio;* and an accounting for the damages may still be ordered on behalf of the common stockholders as a class, should other equitable relief be deemed unavailing or impossible of rendition.

Approximately 67,000 shares of the common stock, out of a total of 160,000 shares, have been filed for appaisal, leaving about 93,000 shares which have not been so filed. It is this class, to the extent of some 93,000 shares, that your Petitioner represents by this class action. These shares are held by upwards of five hundred persons and firms scattered throughout the United States. I believe that I, as an attorney in good standing in the Courts of the State of New York since 1927, have the requisite integrity to represent them fairly and adequately under the supervision of the Court. These common stockholders, whom your deponent represents as plaintiff in this action, had vested property rights under the plan of readjustment long before the new common stockholders acquired their shares. As such, they are entitled either to a declaratory judgment that the plan of consolidation was void *ab. initio,* or to judgment for an accounting for the property of which they have been unlawfully deprived. I therefore respectfully pray that my petition for a writ of certiorari be granted.

NATHAN KATZ.

Sworn to before me this
1st day of November, 1951.

JEANETTE OETTINGER
Notary Public, State of New York
No. 24-2944400
Qualified in Kings County
Cert. filed with New York County Clerk Office
Commission expires March 30, 1953

Appendix.

Affidavit of Gustave B. Garfield.

SUPREME COURT OF THE UNITED STATES

October Term, 1951

No. 360

NATHAN KATZ, individually and suing on behalf of himself and all other common stockholders of R. HOE & Co., INC., similarly situated,

Petitioner,

against

R. HOE & Co., INC., *et al.*,

Respondents.

STATE OF NEW YORK
COUNTY OF NEW YORK } ss.:

GUSTAVE B. GARFIELD, being duly sworn, deposes and says:

I am the attorney for the Petitioner herein, duly admitted to practice in this Court.

It has been insinuated by Respondents that I have filed this petition without the knowledge and consent of the Petitioner (Respondents' brief, 13, 14). The insinuation is false.

It has been stated by Respondents' attorney

> "not only has petitioner gone far outside the record, but he and his counsel have even gone to the extreme of manufacturing out of whole cloth a quotation from

> Wormser on The Disregard of the Corporate Fiction (p. 18). The language there attributed to Wormser was never uttered by him."

I deny the accusation and assert that there is no foundation whatsoever for this baseless attack against my integrity. I have not gone outside the record nor did I manufacture a quotation from Wormser. I did not quote Wormser in the Petition for a Writ, at all. I merely cited him as authority.

It is perhaps because Respondents' counsel, Neil P. Cullom has been criticized by the New York Appellate Division, First Department, in the case of *Pelzer* v. *Perry*, 203 App. Div. 58, p. 60 [1922], because he "has adverted to a matter that formed no part of the record on these appeals, and used intemperate and impertinent language" that he seeks to cast me in the same role in which he has been thus judicially cast. Though he was in that same decision then "admonished that a repetition of the offense will call for more drastic action", he nevertheless continues the same pattern of behavior.

An examination of the matter quoted at page 18 of the Petition shows that it was there stated as the point made by me "in every State Court to which the matter has been submitted." The quoted matter is from my own briefs below and is as follows:

> "The Court should pierce the corporate veil of the recently formed dummy, Hoe Export Import Corporation, disregard its form as a subsidiary, and regard it in substance as an instrument or device conceived and created by the Class A directors of R. Hoe & Co., Inc. for the sole purpose of the evasion of the law which gives the common stockholders the right to vote upon the proposed consolidation."

How ridiculous and unfair to charge that this sentence was intended to be read by this Court as a quotation from a textbook published in 1927, as stated in the index (p. v.) to the petition!

The same pattern of behavior has been followed by Respondents' attorney throughout this litigation. Thus, in an affidavit submitted by him in opposition to a motion for an injunction *pendente lite,* sworn to on August 23, 1950, Mr. Cullom swore *inter alia:*

> "(B) That the Court at the close of the 77-B bankruptcy proceeding had been inclined to eliminate the common stock completely and, when finally prevailed upon not to do so, had insisted that the charter be so drawn as to give it the absolute minimum of power and security. * * *
>
> "(e) Confiscation of plaintiff's property—The claims set forth in the complaint that the consummation of the plan would involve a confiscation of plaintiff's property in violation of the provisions of the State and Federal Constitution are not only unsound in law, but false in fact. * * *
>
> "If, therefore, plaintiff has any quarrel with the restrictions upon the common stock's right to vote, it is with the Federal Court and not with this management."

After reading Mr. Cullom's affidavit, your deponent ascertained the falsity of its assertion that restrictions placed upon the common stock prevented it from voting upon the proposed amendment which sought to deprive the common stockholders of their cumulative voting rights. Your deponent thereupon orally asserted the falsity of that statement, in his argument before the Appellate Division, First Department; and that Court unanimously

stayed the consummation of the plan pending the trial of the action (see Decision, p. 47, Petition).

Thereafter, petitioner applied to the United States District Court for relief, taking at his word Mr. Cullom's sworn statement that "if plaintiff has any quarrel with the restrictions upon the common stock's right to vote, it is with the Federal Court and not with this management."

Mr. Cullom's answer to this application for relief in the Federal Court was a motion to punish Petitioner and your deponent for contempt of court. This application was of course, denied.

The application for relief in the Federal Court came on before U. S. District Judge McGohey. On the pleadings merely, and without a hearing on the merits, Mr. Cullom moved to dismiss the petition because of a pending appeal from the State Court decision to the Appellate Division, First Department. This motion was granted on November 8, 1950 by Judge McGohey, in an opinion in which he stated *inter alia*

> "The petitioner sought and failed to justify the intervention of the state court. He cannot, while pressing his appeal there, relitigate the same issues in this court."

Petitioner appealed to the United States Circuit Court of Appeals from the order of Judge McGohey, and he was met with a motion to dismiss at the Circuit Court of Appeals upon the following three grounds:

1. That the appeal was academic.
2. That the court lacked jurisdiction.
3. That the petitioner was endeavoring to have this court review the decisions of the state court.

Appendix.

The Circuit Court of Appeals dismissed Petitioner's appeal with a single word "Dismissed". It did not state the ground of its decision. Petitioner thereupon moved for a rehearing on January 19, 1951, praying "that this honorable court in the interest of substantial justice and to clarify the record state the ground or basis of its action in dismissing the appeal." This petition for rehearing was likewise denied by the Circuit Court of Appeals with one word "Denied."

The whole purpose of the petition for rehearing was to render the judgment of dismissal final, so that Petitioner might apply to this court for a writ of certiorari to review the action of the Circuit Court of Appeals. But because the dismissal by Judge McGohey and the motion to dismiss at the Circuit Court of Appeals were predicated upon the assertion that Petitioner was endeavoring to review the judgment of the State court, the orders of neither the Circuit Court of Appeals nor of Judge McGohey had such finality as would permit a review by the United States Supreme Court. The Circuit Court of Appeals, however, denied the motion for a rehearing without specifying the ground of decision.

Now it is asserted falsely by the Respondents

> "Precisely the same Federal questions sought to be raised now have all been adjudicated adversely to petitioner in a suit brought by him, during the pendency of the case at bar, in the Federal court; and the decision of that court is *res judicata.*"

A recital of the foregoing facts makes it clear that there has been no adjudication by the Federal Court on the merits. If there had been Petitioner would assuredly have applied for certiorari to this court from the Circuit Court of Appeals. Petitioner has exhausted all remedies before applying to this court for certiorari.

Finally, an attempt is made to have this court dismiss the appeal upon the asserted ground that the failure to raise the Federal questions at the Trial Court, the Appellate Division and the Court of Appeals, constitutes a waiver and an abandonment thereof.

As shown by the foregoing quotation from Mr. Cullom's affidavit, the Federal question was raised at the very outset of this litigation. Respondents do not controvert Petitioner's statement at page 19 of the petition, referring to pertinent portions of the record to support his contention that the lower court rulings were of a nature to bring the case within the statutory provisions that confer jurisdiction upon this court. Instead, by means of the affidavit of a layman (p. 51 of Respondents' Brief) they assert that the Federal questions were nowhere raised at either the Appellate Division or the Court of Appeals. Your deponent denies this assertion. To avoid an extended controversy, your deponent has procured certified copies of the briefs of the various parties at the Appellate Division, of Petitioner's motion papers and briefs at the Court of Appeals and of Respondents' answering brief. Annexed to this affidavit as addenda are pertinent portions of the said briefs and record showing precisely the nature of the Federal questions raised.

In his reply brief to which this affidavit is annexed, Petitioner has amended the Federal questions presented, merely by paraphrasing the summary of Petitioner's argument as made by Respondents' counsel, in his briefs at the Appellate Division and Court of Appeals. As so amended, the question appears at page 19 of the Reply Brief.

It is well nigh impossible in the course of a necessarily short brief and affidavit, to deal with the many inaccurate and misleading statements in Respondents' brief and affidavit in opposition to this petition, most of which statements are irrelevant to the issues. One such point,

however, is of importance sufficient to require answer. It is made as follows under the headnote "Advantages of the Plan to the Common Stock":

> "2. The consolidation not only eliminated the B stock immediately but will ultimately, through the operation of the sinking fund, eliminate the A stock. Upon the basis of the new capitalization, the common stock will then be the only surviving stock with full rights of ownership and voting control." (Respondents' Brief, p. 10.)

This statement is obviously designed to convey the impression that the class of common stockholders represented by Petitioner will eventually acquire "full rights of ownership and control". It artfully conceals the fact that of the *new* common stock to be issued under the consolidation plan to a number of 546,761 shares, the holders of the entire issue of the *old* common stock are accorded 160,000 shares—a mere 29.2% of such new common stock issue! (R. 561).

If in fact the plan was so beneficial to the common stockholders, it is strange indeed that Respondents were so assiduous in choosing the one procedure calculated to deprive the common stockholders of any right to vote upon it.

The reason for this procedure will be found in the fact that Mr. Cullom stated on June 28, 1950, fully two weeks before the organization of Hoe Export Import Corporation,

> "In view of the impossibility of obtaining the consent of two-thirds of the Common stock on a plan of recapitalization which would meet the approval of the A, he suggested that a consolidation with another

corporation, perhaps a wholly-owned subsidiary, be effected, pursuant to Section 86 of the N. Y. Stock Corporation Law."

There is a crying need for review by this court. The Federal question presented is novel. It was not passed upon by the State courts. It is a question of paramount public importance to the community. It involves the integrity of the decrees of the United States District Court in bankruptcy. It is a case which is in common gossip in financial circles. The public interest would best be served by a review by this court. For the reasons stated in the petition, your deponent respectfully prays that the petition for writ of certiorari be granted.

GUSTAVE B. GARFIELD.

Sworn to before me this
1st day of November, 1951.

JEANNETTE OETTINGER
Notary Public, State of New York
No. 24-2944400
Qualified in Kings County
Cert. filed with New York County Clerk's Office
Commission expires March 30, 1953

Appendix.

Letter from Clerk of the Court of Appeals.

STATE OF NEW YORK
COURT OF APPEALS

(Emblem)
Raymond J. Cannon
Clerk

Clerk's Office
Albany 7

October 23, 1951

Gustave B. Garfield, Esq.
Counselor at Law
122 East 42nd Street
New York 17, N. Y.

Re: Katz v. Hoe & Co.

Dear Sir:

We have your inquiry dated October 16th in which you asked for a certificate from this Court to the effect that Federal Questions were raised and passed upon on your motion for leave to appeal in the above entitled case. We know of no procedure in this Court where such a certification has been or can be made on a motion for leave to appeal. Our usual practice in the past has been to provide counsel with certified copies of the motion papers and briefs presented to the Court on the motion.

We are returning your enclosures to you and will be glad to supply you with a certified copy of your Notice of Motion, Affidavit and Brief upon receipt of our fee of $4.50. We have a printed copy now in our possession to which we can attach our certificate if you so desire.

Very truly yours,

RAYMOND J. CANNON
Clerk

Appendix.

Extracts from Certified Copies of Petitioners' Main Brief at the Appellate Division Showing Federal Questions.

NEW YORK SUPREME COURT

APPELLATE DIVISION—FIRST DEPARTMENT

NATHAN KATZ, individually and suing on behalf of himself and all other common stockholders of R. HOE & Co., INC., similarly situated,

Plaintiff-Appellant,

against

R. HOE & Co., INC., *et al.*,

Defendants-Respondents.

BRIEF OF PLAINTIFF-APPELLANT

* * *

POINT III

The real purpose for the organization of Hoe Export-Import Corporation was to use it as a fraudulent device to deprive the common stockholders of Hoe of their right to take over the ultimate control of Hoe from the "A" stockholders, under the provisions of the plan of readjustment in bankruptcy, without affording the common stockholders the right to vote thereon. The Federal Court's decrees being judgments *in rem*, are *res judicata* and are binding on all Courts, parties and their privies.

On *March 1st, 1935,* a decree was entered in the United States District Court for the Southern District of New York in proceedings captioned, "*In the Matter of R. Hoe*

& Co., Inc., Debtor," File No. 60162, pursuant to Section 77-B of the United States Bankruptcy Act, approving, as filed, a plan of readjustment of the said defendant, R. Hoe & Co., Inc., which was just emerging from insolvency (1288-1302) (Plaintiff's Exhibit 1).

On *April 26th, 1935,* a decree was entered in the United States District Court for the Southern District of New York, declaring the plan of readjustment effective and binding on all creditors and stockholders, it appearing that two-thirds of each class of creditors and stockholders had assented thereto in writing (Plaintiff's Exhibit 2) (1303-23).

On *May 15th, 1935,* a decree was entered in the United States District Court for the Southern District of New York, approving a proposed amendment to the certificate of incorporation of the debtor, R. Hoe & Co., Inc., which conformed to the provisions of the decree and the plan dated March 1st, 1935 (1387-98) (Plaintiff's Exhibit 4).

On *June 25th, 1935,* the United States District Court signed its decree discharging the debtor, R. Hoe & Co., Inc., from all of its debts and obligations or rights of its stockholders except such as were reserved in the plan of readjustment dated March 1st, 1935 (Plaintiff's Exhibit 3) (1330-1398).

The provisions of the plan of readjustment of the debtor, R. Hoe & Co., Inc., as they affect the rights of the parties to this litigation and establish their vested property rights are contained in Article IV, Section 1, page 23, under the sub-heading "Miscellaneous."

We shall endeavor to fairly summarize the provisions of this article as follows:

1. The certificate of incorporation shall be amended so as to provide that the board of directors of the com-

pany shall consist of eleven members. (Previously it had been ten.)

2. Prior preferred stock and preferred stock had been issued under the plan to take care of the rights of certain creditors. It was provided that during such periods of time that the prior preferred stock shall have the right voting cumulatively, to elect and continue in office six members out of the eleven members of the board of directors, the Class A stock, voting cumulatively as a class, shall be entitled to elect and continue in office the other five members of the board of directors. (Obviously, during this period of time, the common stockholders were to have no right to elect any directors.)

3. Upon the termination of the right of the prior preferred stock to elect and continue in office six members of the board of directors (which for our purposes we may assume to be the date of the retirement and payment of the said stock of all preferred stock prior to the Class A stock) and continuing until all accumulated and unpaid dividends are paid on the Class A stock in full through the last quarterly dividend period, the holders of the Class A stock, voting cumulatively as a class, shall be entitled to elect and continue in office nine members of the board of directors, and the holders of the common stock, voting cumulatively as a class, shall be entitled to elect and continue in office two members of the board of directors.

4. After all accumulated and unpaid dividends have been paid on the Class A stock, the common stock shall elect six members out of the eleven members of the board of directors and the Class A stock, five mem-

bers. The right so to elect a majority of the board of directors is referred back to the cumulative voting rights in the original certificate of incorporation, paragraph "Thirteenth" thereof, and is specifically stated to be a cumulative voting right.

5. The voting rights with respect to all matters shall be vested at all times exclusively in the Class A stock, other than the election of directors, except that the common stock shall be entitled to vote with respect to a voluntary dissolution; *provided however*

(a) After all accumulated and unpaid dividends on the Class A stock are paid through the last quarterly dividend period and thereafter, so long as the company is not in default in four or more quarterly dividends on the Class A stock (consecutive or not) the common stock, voting as a class, shall have equal rights with the Class A stock, voting as a class, on all matters other than the election of directors.

(b) The exclusive voting rights vested in Class A stock, other than the election of directors, is also subject to the *further proviso* that except with the consent of the majority of the common stock, no amendment of the certificate of incorporation shall be made which shall impair the right of the common stock, voting as a class, to elect and continue in the office two members of the board as such board shall be constituted from time to time, or which shall impair the class voting rights of the common stock on matters other than the election of directors conferred upon it by the foregoing provisions of this sentence.

Under the plan of readjustment, upon the retirement and payment of the preferred stock the common stockholders

voting cumulatively as a class became entitled to elect and continue in office two members of the board of directors; further it was provided that except with the consent of the common stockholders, no amendment of the certificate of incorporation shall be made which shall impair the right of the common stock, voting cumulatively as a class, to elect two members of the board or which shall impair the class voting rights of the common stock on matters other than the election of directors.

THE RETIREMENT OF THE PREFERRED STOCK

The retirement of the preferred stock was accomplished on September 30, 1946. This appears from the annual report of the defendant (Exhibit O) in which the president of the defendant, Joseph L. Auer, stated:

> "For the first time since R. Hoe & Co., Inc., became a publicly-owned enterprise in 1924, the company is entirely free of long-term debt and has no bonds, *preferred stock* or bank loans outstanding. * * *
>
> "*Thus, the Class A stock has become the senior security of the company,* with operating expenses and current obligations alone having prior claims against assets and income. * * *
>
> "*Of equal significance, with the complete elimination of all debt and preferred stock* was the attainment of the highest level in many years of the book value of the Class A stock, * * *."

Therefore, since September 30, 1946, the common stock under the plan of readjustment, voting cumulatively as a class, has been, and still is, entitled to elect and continue in office two members of the board of directors and to vote upon the amendment to the certificate of incorporation as

proposed in the consolidation certificate. The common stockholders complain that they have been deprived of cumulative voting rights and of the right ultimately to take over the control of Hoe from the A stockholders when the B stock shall have been redeemed.

The Trial Court entered an order, duly appealed from, which denied the plaintiff's motion for a new trial upon rulings of law applicable to the federal decrees as follows:

(a) The Trial Court has failed to take cognizance of the Plan of Readjustment of the United States District Court 77B proceedings and the orders of the said Court dated March 1st, 1935, April 26, 1935, and June 25, 1935, which provide that the common stockholders shall elect two directors voting cumulatively; shall have equal voting rights with the A stockholders on all matters other than the election of directors; and that the certicate of incorporation of R. Hoe & Co., Inc., debtor, shall not be amended without the consent of the common stockholders voting as a class (147).

(b) The controlling decision of the Supreme Court of the United States, *Stoll* v. *Gottlieb,* reported in 305 U. S. 675, reversing *Gottlieb* v. *Crowe,* 368 Ill. 88, which case as decided by the said Supreme Court of the United States, holds that the courts of the several states must give effect as *res adjudicata* to the terms and provisions of a plan of readjustment under a proceeding in 77B, and that said plan is not subject to collateral attack and that by the Court's decision it collaterally attacks and voids as if it never existed, the plan of readjustment contained in the order of March 1, 1935 (148).

In *Stoll* v. *Gottlieb*, *supra*, the Supreme Court of the United States said as follows:

> "This certiorari was allowed to review a judgment of the Supreme Court of Illinois. That court had denied effect to a plea of *res judicata* arising from orders of a district court in bankruptcy. Provisions declaring the supremacy of the Constitution and the extent of the judicial power and authorizing necessary and proper legislation to make the grants effective confer jurisdiction upon this Court to determine the effect to be given decrees of a court of the United States in state courts. As the contention is that the ruling below disregarded decrees of a court of the United States it raised a federal question reviewable under Section 237 (b) of the Judicial Code, 28 U. S. C. A., Section 344 (b).
>
> "The Congress enacted, as one of the earlier statutes, provisions for giving effect to the judicial proceedings of the courts. This has long had its present form. This statute is broader than the authority granted by Article Four, Section One, of the Constitution to prescribe the manner of proof and the effect of the judicial proceedings of states. Under it the judgments and decrees of the federal courts in a state are declared to have the same dignity in the courts of that state as those of its own courts in a like case and under similar circumstances. But where the judgment or decree of the federal court determines a right under a federal statute, that decision is 'final until reversed in an appellate court or modified or set aside in the court of its rendition. As this plea was based upon an adjudication under the reorganization provisions of the Bankruptcy Act, effect as *res judicata* is to be given the federal order, if it is concluded it was an effective

judgment in the court of its rendition. The problem before the Supreme Court of Illinois was not one of full faith and credit but of *res judicata.* In this particular case, a federal question was involved. This was the power of the federal courts to protect those who came before them relying upon constitutional rights or rights given, as in this case, through a statute enacted pursuant to constitutional grants of power."

In the instant case the respective classes of stockholders of the debtor, R. Hoe & Co., Inc., the common stockholders as a class and the A stockholders as a class, relying upon rights given them through the bankruptcy statute enacted pursuant to constitutional grants of power, agreed among themselves as to their respective rights in the future to amend the charter of the debtor and to ultimately take over control of Hoe. This, it has been held, is a judgment *in rem* binding upon the debtor corporation and upon all of its stockholders past, present and future.

The Supreme Court of the United States said, in the case of *Gratiot County State Bank* v. *Johnson,* 249 U. S. 248, citing with approval the case of *Durant* v. *Abendroth,* 97 N. Y. 140, which will be quoted later, as folows:

"The adjudication is, for the purpose of administering the debtor's property, that is, in its legislative effect, conclusive upon the world * * *. So far as it declares the status of the debtor even strangers to the decree may not attack it collaterally * * *. But an adjudication in bankruptcy like other judgments *in rem* is not *res adjudicata* as to the facts or as to the subsidiary questions of law on which it is based, except as between parties to the proceeding or privies thereto."

In the case of *Durant* v. *Abendroth*, 97 N. Y. 140, the Court of Appeals of the State of New York, said as follows:

> "So far as the estate of the petitioning bankrupt is concerned, the proceeding is in the nature of a proceeding *in rem* and when the *res* is brought before the Court its adjudication is binding upon the interests of every person whomsoever in that *res*. All persons interested therein must follow it and assert their rights, or be debarred. * * * The general rule as to proceedings *in rem* is that when the property is within the jurisdiction of the Court pronouncing judgment, whether domestic or foreign tribunal, whatever the Court settles as to the right or title or whatever disposition it makes of the property is valid in every country."

In 50 Corpus Juris Secundum, the rule is summed up as follows, at page 554:

> "It has frequently been held that decrees *in rem* are conclusive evidence against all the world of the facts on which they were based, as well as on the status or title of the *res*, and that it will operate as an estoppel in a subsequent action, in respect of the points or questions adjudicated."

In the case of *Horn* v. *Bennett*, 253 App. Div. 630, the Appellate Division, Second Department, said:

> "The appellant's rights as a stockholder were in subordination to those of the corporation, and a judgment against the corporation is competent to establish plaintiff's status (*Stephens* v. *Fox*, 83 N. Y. 313: 1 Freeman on Judgments [5th ed.], Sec. 514). A judgment against the corporation, unless impeached, is conclusive against the corporation and its stockholders

(*Denike* v. *N. Y. & R. Lime, etc., Co.*, 80 N. Y. 599; *Alexander* v. *Donohoe*, 143 *id.* 203; *Marin* v. *Augendahl*, 247 U. S. 142, 150; *Selig* v. *Hamilton*, 234 *id.* 652; *Royal Arcanum* v. *Green*, 237 *id.* 531; *Levy* v. *Equitable Trust Co.*, 271 Fed. 49)."

It has been held that in the absence of a reservation in the final decree in 77B proceedings, of a power to change or modify a plan previously confirmed and consummated, that not even the Court making the order has jurisdiction to modify it or the plan approved thereunder. See *In rem Tom Moore Distillery Co.*, 52 Fed. Supp. 938; *Re Argyle Lake Shore Corp.*, 98 Fed. 2d 372; *Re Corona Radio & Television Corp.*, 102 Fed. 2d 959 (7th Ill. C. C. A.); *Re Flatbush-Nevins Street Corp.*, 133 Fed. 2d 760 (2nd N. Y. C. C. A.).

Even where the Court has receved jurisdiction with respect to matters which might arise in the consummation of the plan where as here the decree fixed the rights of the parties now before this Court, it was held that the Court which originally made the order in the 77B proceeding did not have jurisdiction thereafter to modify the rights of the parties or to amend the plan so as to change rights which were vested thereunder. Thus in the case of *Re Diversey Bldg. Corp.*, 141 F. 2d 65, 55 A.B.R. (N.S.) 716 (144; C.C.A., 7th Ill.), Sparks, Circuit Judge, said:

"We cannot accept appellant's interpretation of subsection (f) of this Act. We are convinced that Congress did not intend that a debtor-corporation should be permitted to ask for a radical change of plan of reorganization after it had been confirmed by the Court and was being executed under the Court's supervision. It is quite true that the quoted language from subsection (f) states that changes and modifications may

be proposed before or after a plan is confirmed; however, this sub-section must be construed with other pertinent sub-sections, such as (g) and (h), in determining the intention of Congress. *Here the plan as confirmed had been in operation for almost eight years, without complaint so far as this record shows, and it was originally proposed by the debtor itself. Under these circumstances we think the Court was without jurisdiction to entertain appellant's motion. We interpret sub-section (f) to mean that changes and modifications after the plan is confirmed refer to such changes as will better aid in carrying out the plan which has been finally confirmed, and not such changes or modifications as will materially alter the property rights established by the decree of confirmation, and in no event shall any change be made without the consent of the Court.*

"In support of its contention, appellant relies on *In re H. W. Clark Co.* (C.C.A. 7th Cir.), 79 F. 2d 681; *Downtown Invest. Asso.* v. *Boston Metropolitan Bldgs.* (C.C.A. 1st Cir.), 81 F. 2d 314, 30 A.B.R. (N.S.) 483; and *In re Celotex Co.* (D.C.), 12 F. Supp. 1. These cases relate to amendments of the plan of reorganization before its consummation, and for that reason we think they are not in point. We find no authority supporting appellant's interpretation of sub-section (f). Carried to its ultimate conclusion we think it would end in confusion worse confounded both for the creditor and the debtor.

"Appellant urges that the decree of June 28th, 1935, was not a final decree in that the case was not finally disposed of. That decree, however, was interlocutory in its character, and definitely fixed all the rights of the parties, and it was a final and appealable decree. True, the terms of the trust indenture were not fully

performed, and, indeed, full performance could not be required until 1950. However, *the property rights were fixed,* there was no failure of performance on the part of the debtor and its guarantor, and there was no indication that there would be such failure until the principal of the debt was due. Under these circumstances we think that neither the debtor nor the Court could alter those property rights as fixed by the interlocutory decree."

"The district court did not indicate the basis for its ruling. However, we think it was without jurisdiction to grant the relief prayed for."

Perhaps the most recent and the most enlightening case on the subject now under consideration by this Court, is the case of *In re Pittsburgh Terminal Coal Corp.*, appearing in the Federal Advance Sheets of September 25th, 1950, and cited therein as 183 F. 2d 520 (C.C.A. 3d Cir. Pa.), certiorari denied, December 11, 1950, #351, Vol. 95, Law Ed. 179. In that case the Circuit Court of Appeals unanimously affirmed an order of the District Court which granted an application for a preliminary injunction against the holding of a special meeting of stockholders of the debtor corporation called for December 12th, 1949. The purpose of this meeting was to extend the debtor's period of existence and to increase the salary limit of its officers and directors which by its by-laws, written under the plan of reorganization approved by the District Court, limited it to an existence of five years which could be extended for an additional five years, and provided for a limitation on salaries of officers of not to exceed $5,000 per year.

Judge McLaughlin, writing for the unanimous Court, said:

"On December 9th, 1949, after hearing the matter, the District Court preliminarily enjoined the meeting

and ordered the Trustee to investigate appellant for the purpose of determining whether it had been conducted in accordance with the Coal Company plan of reorganization. This appeal is from that order.

"Appellant contends that the District Court had no jurisdiction over it; that the Trustee had no right or duty to supervise its affairs; that the proposed amendments to its by-laws are lawful, and that Court approval is not necessary to their adoption by the stockholders.

"* * * The appellant successor corporation was created in order to liquidate the remaining assets of the debtor. To prevent undue prolongation of the liquidation process and excessive expense in that connection, appellant was given the limited existence of five years, with a possible extension of five more years after that, and a salary ceiling of $5,000.00 a year for all corporate officers and directors. Those provisions were inserted in the by-laws. Appellant's theory is that the increasing of the duration of the corporate existence and the removal of the salary restriction merely means a technical change in the by-laws and that it is entirely a matter of intra-corporate policy having nothing to do with the reorganization plan and its rightful functioning.

"The situation is not as simple as that. The charge is directly made that the person controlling the appellant is endeavoring to defeat an important element of the plan. * * *

"The investigation was authorized and directed 'for the purpose of determining whether or not said corporation has been conducted in accordance with the terms, provisions, intent and purpose of the plan of reorganization of Pittsburgh Terminal Coal Corp.,

debtor.' Report of the investigation is to be made to the Bankruptcy Court. * * *

"The charges concern an important phase of the plan which is still in the process of being carried out. It was part of the plan to accomplish its purpose that appellant was created. If appellant now seeks by the proposed change in its by-laws to violate the letter and the spirit of the plan, the facts should be examined, and while they are being examined appellant should be prevented from doing the very acts which are protested. * * * The charges that appellant is deliberately attempting to evade the plan are serious and substantial."

Summarizing the foregoing orders of the U. S. District Court for the Southern District of New York, and the law applicable thereto in the enforcement of those orders, we arrive at the following conclusion: The debtor-corporation, R. Hoe & Co., Inc., in order to be discharged from the 77B proceeding, had to have the consent of two-thirds in number and amount of its creditors and each class of its stockholders affected by the plan of reorganization. By the plan of reorganization finally approved, control of the corporation passed to the Class A stockholders, they having the right to elect nine out of the eleven directors while the common stockholders had the right to elect two directors. This situation was augmented by an additional provision which gave the common stockholders the right to vote only on the proposition of dissolution and not to vote upon the proposition of consolidation; but such limitations on the rights of the common stockholders to vote were provisional and the provision is incorporated in the plan of reorganization as follows:

"provided, however, that after all accumulated and unpaid dividends on the Class 'A' stock are paid in

full through the last quarterly dividend period and thereafter so long as the Company is not in default in four or more quarterly dividends on the Class 'A' stock (whether consecutive or not), the Common Stock, voting as a class, shall have equal rights with the Class A stock, voting as a class, on all matters other than the election of directors; and provided, further, that except with the consent of a majority of the Common Stock, no amendment of the certificate of incorporation shall be made which shall impair the right of the Common Stock voting as a class to elect and continue in office two members of the Board of Directors as such Board shall be constituted from time to time, or which shall impair the class voting rights of the Common Stock on matters other than the election of directors conferred upon it by the foregoing provisions of this sentence."

The A directors being representatives of the Federal Court were fiduciaries in respect to the common stockholders. Though the common stockholders were the owners of Hoe, the Bankruptcy Court placed the A stockholders in temporary control as its representative, to protect their investment. The temporary control was given to the A stockholders not as owners but as trustees. Their tenure was specifically defined and was to end as soon as their arrearages were paid. That was clearly the intent of the bankruptcy reorganization and was followed for many years.

The present group of A directors took office pursuant to that reorganization plan and as trustees for the Bankruptcy Court in 1946 when the preferred stock was eliminated. Their trusteeship was similar to a spendthrift trust in which the beneficiary (the common stockholders) is protected until he reaches a sound financial position

(arrearages paid off). In establishing this trust and depriving the common stockholders of many of their rights of ownership during its existence the Bankruptcy Court did not grant power to the trustees to extend its duration —at least not without the consent of the common stockholders. Nevertheless, that is exactly what the A stockholders have accomplished here. Not only have they extended the duration of the trust but they appropriated much of the beneficiary's interest therein.

Ordinarily, trustees who appropriate the beneficiary's interest for their own use are guilty of despicable crimes. The A stockholders and directors as trustees have done the same thing here, but because they have covered their criminal act with a cheesecloth (the consolidation) the Trial Court not only did not consider it a crime but held it to be perfectly legal.

This Court should not permit itself to be blinded from the true facts and should recognize the gross breach of fiduciary duty of the A directors.

Since the decrees in the Bankruptcy Court are *res judicata* in the State Court, the provisions thereof are in full force and effect, assuring the common stockholders the right to vote cumulatively as a class upon all matters other than the election of directors as well as upon the amendment of the certificate of incorporation.

The plaintiff was entitled to a judgment on behalf of the common stockholders declaring that the action of the class A directors and stockholders violated a vested property right of the common stockholders contained in the decrees of the United States District Court; that the decrees of the District Court upon the basis of which the debtor, R. Hoe & Co., Inc., was discharged from bankruptcy are binding upon the debtor and the respective classes of stockholders and their privies. Plaintiff's pro-

posed findings of fact (94-107) should be signed by this Court and declaratory judgment should enter, holding that the action of the directors and the A stockholders in effecting the consolidation was null and void as matter of law.

* * *

In the instant case, the common stockholders' right to vote is completely destroyed by the fictitious consolidation. The right to vote is an essential attribute of the common stockholders' property, and the deprivation thereof without compensation is illegal.

> *Lord* v. *Equitable Life Assur. Society,* 194 N. Y. 212.

There is a tremendous difference between a right to vote and a right to dividends. The former is the only means that the stockholder has to supervise and control his property.

> *Lord* v. *Equitable Life Assur. Society, supra.*

Dividends, on the other hand, are entirely within the discretion of the Board of Directors and stockholders have no vested rights thereto until actually declared.

The elimination of arrearages in dividends on preferred stock was also involved in the *Hottenstein* and *Zobel* cases, *supra.* In the former, the Federal Court held that it was bound to follow the Delaware law as determined by the Delaware Court in the *Havender* case, *supra.* In the latter, the Court relied almost entirely upon the decisions in *Havender* and *Hottenstein, supra.*

In none of the cases cited by the defendants did the consolidation circumvent any other provision of the law, as here; in none did the Court sanction the disfranchisement of a class of stockholders by resort to subterfuge.

CONCLUSION.

The judgment and order appealed from should be reversed, plaintiff's proposed findings signed, and judgment entered in favor of the plaintiff and defendant-appellant, Martin, *for the relief demanded in the complaint* and cross complaint with costs and disbursements to the appellants. The certificate of consolidation should be declared a nullity and the Secretary of State directed to strike the certificate of consolidation from his records. The shares of stock issued pursuant to the plan of consolidation should be declared null and void and the common stockholders, as they existed prior to the consolidation, should be reinvested with all of the rights given to them under the plan of readjustment and under the certificate of incorporation as amended prior to consolidation.

Respectfully submitted,

GUSTAVE B. GARFIELD,
Attorney for Plaintiff-Appellant.

Appendix.

Extract from Certified Copies of the Respondents' Brief at the Appellate Division (p. 62 thereof) Showing Its Summary of Federal Question.

"POINT VI

"THERE HAS BEEN NO VIOLATION OF THE FEDERAL COURT ORDERS.

In his brief (p. 20), Katz argues that this consolidation violates the plan of reorganization approved by the Federal Court in the Hoe 77B proceeding of 1935—or, to state it differently, that the certificate of incorporation, as amended and approved by that court when the debtor was discharged in 1935, immutably defines the rights of the stockholders; and cannot later be amended or altered in any respect or by any means. To state the claim is to answer it.

The Trial Court dismissed the contentions as unsound; and it is worthy of note that Katz's colleague, Martin, does not say one word in support thereof. * * *"

Appendix.

Extracts from Certified Copies of Petitioner's Reply Brief Showing Federal Questions Raised.

NEW YORK SUPREME COURT

APPELLATE DIVISION—FIRST DEPARTMENT

NATHAN KATZ, individually and suing on behalf of himself and all other common stockholders of R. HOE & CO., INC., similarly situated,

Plaintiff-Appellant,

against

R. HOE & CO., INC., *et al.*,

Defendants-Respondents.

REPLY BRIEF OF PLAINTIFF-APPELLANT

The issues presented by this appeal are of far reaching importance to the financial community at large. They are invested with a public interest which affects investors small and large throughout the entire length and breadth of the land. Our metropolis is the financial center of the world and what we do and say here is listened to and watched by every financial paper and advisor everywhere. These people want to know whether Cullon can get away with it. These people are clamoring to find out whether a group of directors domiciled in the Bronx, can, by means of a paper device of a corporate fiction, set at nought the sovereign will of the People of the State of New York, and the solemn decree of the United States District Court discharging the debtor R. Hoe & Co. from insolvency.

The Supreme Court of the United States in the case of *Stoll* v. *Gottlieb,* 305 U. S. 675, has held that a decree of the bankruptcy court, discharging an insolvent from

77B proceedings, must be respected by state courts as *res judicata,* as to the legislative aspects of the plan of readjustment. Defendant Cullon has invented a new law. He is not bound by the Supreme Court of the United States. He is the law unto himself. He says that the decision rendered by Judge McGohey dismissing plaintiff's appeal to that court for lack of jurisdiction of the Federal Court is *res judicata* in this court. That's a new wrinkle in the annals of legal legerdemain, *i. e.,* to ignore the original decree of a court as *res judicata* and to plead as an adjudication that court's refusal to take jurisdiction because prior action was commenced in a state court.

Defendants-respondents assert that there has been no violation of the Federal Court orders (Point VI). But in making this point they utterly disregard the decision of the Supreme Court of the United States in *Stoll* v. *Gottlieb, supra,* and the implication of that decision. Instead they content themselves by quoting a fragment from the decision of the Circuit Court of Appeals for the Second Circuit *In re Ambassador Hotel Corp.,* 2 Cir., 124 F. 2nd 435, 437. It is noteworthy that the Circuit Court has, on February 1, 1951, repudiated limited and explained the scope of its decision in the *Ambassador* case. See N. Y. Law Journal (front page) March 5, 1951, *Prudence Bonds Corp.* v. *City Bank Farmers Trust Co.,* where L. Hand, C. J., writing for the unanimous bench said:

"• • • there has undoubtedly been considerable difference of opinion about the court's power to accommodate the original 'plan' to changes after confirmation in the financial situation of the 'revived debtor.' On this question we declared ourselves four times between 1942 and 1946. In In re Ambassador Hotel Corporation (124 Fed., 2d, 435) the State of New York had passed the 'Streit Law' affecting voting trusts after a 'plan' had been confirmed which set up

a voting trust, whose duration, though lawful at the time, it was alleged that that act had cut down. We held that the state courts alone had jurisdiction to decide whether it had done so, and we did not mention the circumstance that the order of confirmation contained no reservation of powers, so far as appears. * * *

* * * We therefore conclude that our earlier decisions, in so far as they depended upon the presence of an express reservation in either the 'plan' or the order of confirmation, were erroneous.

The question is one of discretion, though of a discretion which should be sparingly exercised, and which should not be exercised, as in North American Car Corporation v. Peerless Machine Corporation (143 Fed., 2d, 938, C. A. 3), unless the circumstances peremptorily demand it. That they did in Knight v. Wertheim & Co., 158 Fed. (2), 838, for otherwise the bondholders would have gone off with a large equity, owing to the wholly unexpected appreciation of the property, a result which the whole history of foreclosure forbade. We cannot deny that the view which we now take may lead to abuse; it is often exceedingly difficult for a bankruptcy court to resist the importunities, usually unopposed, of those who wish to keep the 'revived debtor' indefinitely beneath its aegis, and our review of a discretion which we may think to have been unwisely exercised is not a very effective remedy. We can do no more than declare, for whatever weight it may have, that we deem the long delay which so often occurs between the order of 'confirmation' and the 'final order' a major abuse, and that a judge who superintends such a proceeding should feel himself charged with an affirmative duty to insist upon its early conclusion."

It is therefore clear that the decision of the Circuit Court for the Second Circuit in dismissing the appeal of appellant Katz, without the record before it, merely refused as a matter of discretion to take jurisdiction. Since plaintiff prayed only for an injunction in that court and not as here for a declaratory judgment the court may have dismissed the case for mootness, but refused to express itself. Here this court is asked to declare the illegal acts done by defendants-respondents to be such even though the meeting of A stockholders may already have been held. Survival of the dispute is clear in this court and the question is not moot.

* * *

When the defendant R. Hoe & Co., Inc., was an insolvent, in 1935, represented by an eminent firm of attorneys (Simpson, Thatcher and Bartlett), it came, hat in hand, into the United States District Court for the Southern District of New York, pleading for release from the economic drought which engulfed it. It made a compact with its common stockholders, past, present and future, that at a time to come, when its obligations to its creditors and "A" stockholders had been fulfilled, the common stockholders, would come into their own and taken over control. This compact is contained in the miscellaneous provision of the plan of readjustment, dated March 1, 1935, which has been quoted in our main brief and in the complaint.

In the intervening 15 years since the defendant R. Hoe & Co., Inc., has been discharged from bankruptcy, many investors have paid their hard earned money for its common stock.

The common stockholders of Hoe had a right to rely upon the court decrees and the charter provisions which gave them the right to vote on all matters, including the amendment of its Certificate of Incorporation on an equality with the "A" stockholders.

* * *

Appendix.

Extract from Certified Copies of Petitioner's Notice of Motion for Leave to Appeal to the Court of Appeals Showing Federal Questions.

COURT OF APPEALS OF THE STATE OF NEW YORK

NATHAN KATZ, individually and suing on behalf of himself and all other common stockholders of R. HOE & Co., INC., similarly situated,

Plaintiff-Appellant,

against

R. HOE & Co., INC., *et al.*,

Defendants-Respondents.

SIRS:

PLEASE TAKE NOTICE that upon the annexed affidavit of GUSTAVE B. GARFIELD, sworn to May 15, 1951, upon the notice of motion and brief of the defendant-appellant Martin for leave to appeal to the Court of Appeals, intended to be served and heard simultaneously herewith, and upon the annexed plaintiff-appellant's brief, the undersigned will move this court at a term thereof to be held at the Court of Appeals, Albany, New York, at the first term for the hearing of motions after the service and filing of the within papers, for an order granting leave to the plaintiff-appellant to appeal to the Court of Appeals from a judgment of the Supreme Court, New York County, made and entered in the office of the Clerk of the County of New York on April 27, 1951, which adjudges that the judgment in favor of the defendants except Martin dismissing the complaint and cross-complaint and the order

denying plaintiff's motion for a new trial be in all things affirmed, and plaintiff will also move for leave to appeal from the order of the Appellate Division, First Department, dated the 25th day of April, 1951, as unanimously affirms the judgment appealed from, on the following grounds:

* * *

4. The real purpose for the organization of Hoe Export-Import Corporation was to use it as a fraudulent device to deprive the common stockholders of Hoe of their right to take over the ultimate control of Hoe from the "A" stockholders, under the provisions of the plan of readjustment in bankruptcy, without affording the common stockholders the right to vote thereon. The Federal Court's decrees, being judgments *in rem*, are *res judicata* and are binding on all Courts, parties and their privies.

5. This Court should pierce the corporate veil of "the recently formed" dummy, Hoe Export-Import Corporation, disregard its form as a subsidiary, and regard it in substance as an instrument or device conceived and created, by the Class A directors of R. Hoe & Co., Inc., for the sole purpose of the evasion of the law which gives the common stockholders the right to vote upon the proposed reorganization.

Yours, etc.,

GUSTAVE B. GARFIELD,
Attorney for Plaintiff-Appellant,
Nathan Katz,
Office and Post Office Address,
122 East 42nd Street,
New York City, N. Y.

To:

NEIL P. CULLOM, Esq.,
Attorney for Defendants-Respondents,
Office and Post Office Address,
63 Wall Street,
New York City, N. Y.

BOOTH & BARON, Esqs.,
Attorneys for Defendant-Appellant, Martin,
20 Broad Street,
New York City, N. Y.

THE CLERK OF THE COURT OF APPEALS.

Affidavit of Gustave B. Garfield.

COURT OF APPEALS OF THE STATE OF NEW YORK.

NATHAN KATZ, individually and suing on behalf of himself and all other common stockholders of R. HOE & Co., INC., similarly situated,

Plaintiff-Appellant,

against

R. HOE & Co., INC., *et al.*,

Defendants-Respondents.

City, County and State of New York, ss:

GUSTAVE B. GARFIELD, being duly sworn, deposes and says:

I am the attorney for the plaintiff-appellant herein.

* * *

It is the appellant's contention that the muddled financial situation of the defendant, R. Hoe & Co., Inc., and those who purchased the new shares of stock issued after the consolidation, was brought about by the failure of the Appellate Division to grant a stay pending an appeal.

The case was tried upon the theory that if a single common stockholder had a just cause of action and a right to vote, his right is enforceable notwithstanding the demand of the A stockholders or the wishes of the remaining common stockholders. It is submitted that the Appellate Division could not change the theory upon which the case was tried and affirm as a matter of convenience. If a wrong was done to one it was done to all stockholders in that class.

Appellant submits that it is a greater injustice to permit a consolidation, effected contrary to the edict of the legislature and the solemn decree of the bankruptcy court than it is to upset it because the transaction is fully consummated. Those who purchased shares after consolidation purchased it subject to pending litigation and an appeal of which the whole world had notice.

The basic question raised by this appeal is one of law. The basic facts were not disputed upon the trial nor can they be disputed upon this appeal. It is only the legal interpretation which one places upon conceded facts which is in controversy.

It is respectfully submitted that a question of paramount and substantial public interest is presented, which should be decided by this Court.

Plaintiff urges that a common stockholder is not compelled to accept appraisal in a larcenous consolidation and that appraisal is not the exclusive remedy of a common stockholder who seeks to protect his vested right in com-

mon with all other stockholders to take over the control of a corporation from its temporary trustees, the A stockholders.

There is more involved in this case than money. The integrity of the bankruptcy court and of the State of New York, which has issued these shares of stock pursuant to a bankruptcy decree and under a New York charter, is involved. The legislative mandate that every common stockholder is entitled to vote on a proposed change of corporate charter affecting stockholdings has been thwarted by a cheap device. Stockholders throughout the land await the decision of this Court on this important matter. It is respectfully submitted that the case should be fully aired in this court and for that reason it is respectfully prayed that the plaintiff's motion for leave to appeal be granted.

* * *

GUSTAVE B. GARFIELD.

Sworn to before me this
15th day of May, 1951.

JEANNETTE GETTINGER,
Notary Public, State of New York.

Appendix.

Extracts from Brief of Plaintiff-Appellant Nathan Katz in Support of Motion for Leave to Appeal to the Court of Appeals Showing Federal Questions.

COURT OF APPEALS OF THE STATE OF NEW YORK

NATHAN KATZ, individually and suing on behalf of himself and all other common stockholders of R. Hoe & Co., Inc., similarly situated,

Plaintiff-Appellant,

against

R. HOE & CO., INC., JOSEPH L. AUER, HARRY K. BARR, VANDIVER BROWN, WILLIAM L. CANADY, NEIL P. CULLOM, HAROLD W. DANSER, EDWARD FOSTER, JOHN KADEL, EDWIN L. MUNZERT, HAROLD M. TILLINGHAST, DANIEL BEISINGER, WILLIAM F. BYRNE, ARTHUR DRESSEL, CHARLES A. HARLESS, JOHN R. KINGAN, CHARLES E. LITTLETON, W. J. V. MURPHY,

Defendants-Respondents,

and

ALFRED D. MARTIN,

Defendant-Appellant.

Statement.

The plaintiff-appellant Nathan Katz moves for leave to appeal to this court after unanimous affirmance by the Appellate Division, First Department, of his appeal to that court. Suing individually and on behalf of all other common stockholders of R. Hoe & Co., Inc., plaintiff ap-

pealed from a judgment made and entered in the office of the Clerk of the Supreme Court, New York County, dated October 31, 1950, after trial before Honorable Denis O'Leary Cohalan, dismissing on the merits the plaintiff's complaint and the cross complaint of the defendant, Alfred D. Martin, in an action seeking a declaratory judgment. Plaintiff also appealed from an order entered on or about November 3, 1950, denying plaintiff's motion for a new trial (14-18, 145-152).*

The Second Amended Complaint.

At the time of the trial, the defendant, R. Hoe & Co., Inc., a domestic corporation, was capitalized as follows (26):

Title of Shares	Par Value	Shares Authorized	Outstanding
Class A	$10.00 per share	100,000	95,997
Class B	.10 " "	194,767	194,767
Common Stock	1.00 " "	160,000	160,000

Plaintiff is the owner of 500 shares of the common capital stock of the corporation; defendant, R. Hoe & Co., Inc., having acquired his shares December 23, 1949 (35).

The defendant, R. Hoe & Co., Inc., was reorganized under § 77-B of the Bankruptcy Act in the United States District Court for the Southern District of New York, pursuant to a plan of readjustment, dated March 1, 1935, two-thirds of all classes of stock consenting thereto on

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* Figures in parentheses throughout this brief are to folio references of the record.

April 26, 1935. Thereupon, the debtor was discharged and its property returned to it (27-31).

The plan of readjustment which survived the debtor's discharge in bankruptcy provided prospectively for the voting rights of the A stockholders and common stockholders as follows:

> "The voting rights with respect to all matters other than the election of directors, shall at all times be vested exclusively in the holders of Class 'A' stock, except as in Article III thereof specified as to the prior Preferred Stock and the Preferred Stock, and except that the Common Stock, voting as a class, shall be entitled to vote only with respect to a voluntary dissolution of the company pursuant to Section 105 of the Stock Corporation Law of New York; *provided,* however, that after all accumulated and unpaid dividends on the Class 'A' stock are paid in full through the last quarterly dividend period and thereafter so long as the company is not in default in four or more quarterly dividends on the Class 'A' stock (whether consecutive or not) the Common Stock, voting as a class, shall have equal rights with the Class 'A' Stock, voting as a class on all matters other than the election of directors, and *provided further* that, except with the consent of a majority of the Common Stock, no amendment to the Certificate of Incorporation shall be made which shall impair the right of the Common Stock voting as a class to elect and continue in office two members of the Board of Directors as such Board shall be constituted from time to time, or which shall impair the class voting rights of the Common Stock on matters other than the election of directors conferred upon it by the foregoing provisions of this sentence" (28-30).

Appendix.

A plan of consolidation and recapitalization was put into effect on February 28, 1947, by which all dividend arrears on the Class A stock were eliminated by the issuance to the Class A stock of four shares of non-voting Class B stock, plus $3 in cash for each share of Class A stock held (33).

The Class A stockholders have received and accepted in full payment of all accumulated and unpaid dividends in arrears the four shares of B stock for each share held by them and dividends have been paid on the Class A stock consecutively since February 28, 1947, to date (34).

In or about the month of June, 1950, the A directors entered into a scheme to recapitalize the defendant, R. Hoe & Co., Inc., without permitting the common stockholder to vote upon said recapitalization, for the purpose of taking ultimate control away from the common stockholder and vesting it permanently in the Class A stockholders (36-38).

Pursuant to the said scheme, the directors representing the A stockholders, on July 11, 1950, caused a dummy corporation called "Hoe Export-Import Corporation" to be organized under the laws of the State of New York, which corporation never transacted business, had no assets or reason for existence other than as instrument to carry out the foregoing conspiracy. That the A directors caused a special meeting of the Class A stockholders to be called to vote upon a consolidation between the defendant R. Hoe & Co., Inc., and its dummy subsidiary, Hoe Export-Import Corporation (38-39).

Plaintiff alleges that to permit the defendants to carry out said reorganization and recapitalization under the guise of the aforesaid fraudulent consolidation without permitting the common stockholders to vote thereon, does consti-

tute deprivation of plaintiff's property without due process and a violation of the laws of the State of New York, of the United States of America and of the decree of the United States District Court for the Southern District of New York, dated March 1, 1935, and April 25, 1935; that plaintiff has no adequate remedy at law (41-44).

Plaintiff demands a declaratory judgment that the said action of the defendants is null and void and of no effect in law (45-46).

The Answer of the Defendant-Appellant, Martin.

The defendant, Alfred D. Martin, a director representing the common stockholders, for his answer, sets forth a crossclaim in which he prays for the same relief sought by the plaintiff (49-86).

The Answer of the Defendants Constituting the A Directors and the Defendant Corporation, R. Hoe & Co., Inc.

Aside from admitting that plaintiff is an owner of 500 shares of the common stock of the defendant, R. Hoe & Co., Inc., which were transferred to his name on December 23, 1949, and the making of various orders by the United States District Court for the Southern District of New York, the said defendants deny each and every allegation in the second amended complaint. They further allege that plaintiff has an adequate remedy at law (88-93).

POINT III

The real purpose for the organization of Hoe Export-Import Corporation was to use it as a fraudulent device to deprive the common stockholders of Hoe of their right to take over the ultimate control of Hoe from the "A" stockholders, under the provisions of the plan of readjustment in bankruptcy, without affording the common stockholders the right to vote thereon. The Federal Court's decrees being judgments *in rem*, are *res judicata* and are binding on all Courts, parties and their privies.

On *March 1st, 1935,* a decree was entered in the United States District Court for the Southern District of New York in proceedings captioned, *"In the Matter of R. Hoe & Co., Inc., Debtor,"* File No. 60162, pursuant to Section 77-B of the United States Bankruptcy Act, approving, as filed, a plan of readjustment of the said defendant, R. Hoe & Co., Inc., which was just emerging from insolvency (1288-1302) (Plaintiff's Exhibit 1).

On *April 26th, 1935,* a decree was entered in the United States District Court for the Southern District of New York, declaring the plan of readjustment effective and binding on all creditors and stockholders, it appearing that two-thirds of each class of creditors and stockholders had assented thereto in writing (Plaintiff's Exhibit 2) (1303-23).

On *May 15th, 1935,* a decree was entered in the United States District Court for the Southern District of New York, approving a proposed amendment to the certificate of incorporation of the debtor, R. Hoe & Co., Inc., which conformed to the provisions of the decree and the plan dated March 1st, 1935 (1387-98) (Plaintiff's Exhibit 4).

On *June 25th, 1935,* the United States District Court signed its decree discharging the debtor, R. Hoe & Co., Inc., from all of its debts and obligations or rights of its stock-

holders except such as were reserved in the plan of readjustment dated March 1st, 1935 (Plaintiff's Exhibit 3) (1330-1398).

The provisions of the plan of readjustment of the debtor, R. Hoe & Co., Inc., as they affect the rights of the parties to this litigation and establish their vested property rights are contained in Article IV, Section 1, page 23, under the sub-heading "Miscellaneous," as follows:

1. The certificate of incorporation shall be amended so as to provide that the board of directors of the company, shall consist of eleven members. (Previously it had been ten.)

2. Prior preferred stock and preferred stock had been issued under the plan to take care of the rights of certain creditors. It was provided that during such periods of time that the prior preferred stock shall have the right voting cumulatively, to elect and continue in office six members out of the eleven members of the board of directors, the Class A stock, voting cumulatively as a class, shall be entitled to elect and continue in office the other five members of the board of directors. (Obviously, during this period of time, the common stockholders were to have no right to elect any directors.)

3. Upon the termination of the right of the prior preferred stock to elect and continue in office six members of the board of directors (which for our purposes we may assume to be the date of the retirement and payment of the said stock of all preferred stock prior to the Class A stock) and continuing until all accumulated and unpaid dividends are paid on the Class A stock in full through the last quarterly dividend period, the holders of the Class A stock,

voting cumulatively as a class, shall be entitled to elect and continue in office nine members of the board of directors, and the holders of the common stock, voting cumulatively as a class, shall be entitled to elect and continue in office two members of the board of directors.

4. After all accumulated and unpaid dividends have been paid on the Class A stock, the common stock shall elect six members out of the eleven members of the board of directors and the Class A stock, five members. The right so to elect a majority of the board of directors is referred back to the cumulative voting rights in the original certificate of incorporation, paragraph "Thirteenth" thereof, and is specifically stated to be a cumulative voting right.

5. The voting rights with respect to all matters shall be vested at all times, exclusively in the Class A stock, other than the election of directors, except that the common stock shall be entitled to vote with respect to a voluntary dissolution; *provided however*

(a) After all accumulated and unpaid dividends on the Class A stock are paid through the last quarterly dividend period and thereafter, so long as the company is not in default in four or more quarterly dividends on the Class A stock (consecutive or not) the common stock, voting as a class, shall have equal rights with the Class A stock, voting as a class, on all matters other than the election of directors.

(b) The exclusive voting rights vested in Class A stock, other than the election of directors, is also subject to the *further proviso* that except with the consent of the majority of the common stock, no amendment of the certificate of incorporation shall

> be made which shall impair the right of the common stock, voting as a class, to elect and continue in office two members of the board as such board shall be constituted from time to time, or which shall impair the class voting rights of the common stock on matters other than the election of directors conferred upon it by the foregoing provisions of this sentence.

Under the plan of readjustment, upon the retirement and payment of the preferred stock the common stockholders voting cumulatively as a class became entitled to elect and continue in office two members of the board of directors; further it was provided that except with the consent of the common stockholders, no amendment of the certificate of incorporation shall be made which shall impair the right of the common stock, voting cumulatively as a class, to elect two members of the board or which shall impair the class voting rights of the common stock on matters other than the election of directors.

THE RETIREMENT OF THE PREFERRED STOCK.

The retirement of the preferred stock was accomplished on September 30, 1946. This appears from the annual report of the defendant (Exhibit O) in which the president of the defendant, Joseph L. Auer, stated:

> "For the first time since R. Hoe & Co., Inc., became a publicly-owned enterprise in 1924, the company is entirely free of long-term debt and has no bonds, *preferred stock* or bank loans outstanding. * * *
>
> "*Thus, the Class A stock has become the senior security of the company,* with operating expenses and current obligations alone having prior claims against assets and income. * * *

> *"Of equal significance, with the complete elimination of all debt and preferred stock* was the attainment of the highest level in many years of the book value of the Class A stock, * * *."

Therefore, since September 30, 1946, the common stock under the plan of readjustment, voting cumulatively as a class, has been, and still is, entitled to elect and continue in office two members of the board of directors and to vote upon the amendment to the certificate of incorporation as proposed in the consolidation certificate. The common stockholders complain that they have been deprived of cumulative voting right and of the right ultimately to take over the control of Hoe from the A stockholders when the B stock shall have been redeemed.

The Trial Court entered an order, duly appealed from, which denied the plaintiffs' motion for a new trial upon rulings of law applicable to the federal decrees as follows:

(a) The Trial Court has failed to take cognizance of the Plan of Readjustment of the United States District Court 77B proceedings and the orders of the said Court dated March 1st, 1935, April 26, 1935, and June 25, 1935, which provide that the common stockholders shall elect two directors voting cumulatively; shall have equal voting rights with the A stockholders on all matters other than the election of directors; and that the certificate of incorporation of R. Hoe & Co., Inc., debtor, shall not be amended without the consent of the common stockholders voting as a class (147).

(b) The controlling decision of the Supreme Court of the United States, *Stoll* v. *Gottlieb,* reported in 305 U. S. 675, reversing *Gottlieb* v. *Crowe,* 368 Ill. 88,

which case as decided by the said Supreme Court of the United States, holds that the courts of the several states must give effect as *res adjudicata* to the terms and provisions of a plan of readjustment under a proceeding in 77B, and that said plan is not subject to collateral attack and that by the Court's decision it collaterally attacks and voids as if it never existed, the plan of readjustment contained in the order of March 1, 1935 (148).

In *Stoll* v. *Gottlieb, supra,* the Supreme Court of the United States said as follows:

"This certiorari was allowed to review a judgment of the Supreme Court of Illinois. That court had denied effect to a plea of *res judicata* arising from orders of a district court in bankruptcy. Provisions declaring the supremacy of the Constitution and the extent of the judicial power and authorizing necessary and proper legislation to make the grants effective confer jurisdiction upon this Court to determine the effect to be given decrees of a court of the United States in state courts. As the contention is that the ruling below disregarded decrees of a court ot the United States it raised a federal question reviewable under Section 237 (b) of the Judicial Code, 28 U.S.C.A., Section 344 (b).

* * * * * *

"The Congress enacted, as one of the earlier statutes, provisions for giving effect to the judicial proceedings of the courts. This has long had its present form. This statute is broader than the authority granted by Article Four, Section One, of the Constitution to prescribe the manner of proof and the effect of the judicial proceedings of states. Under it the

judgments and decrees of the federal courts in a state are declared to have the same dignity in the courts of that state as those of its own courts in a like case and under similar circumstances. But where the judgment or decree of the federal court determines a right under a federal statute, that decision is 'final until reversed in an appellate court or modified or set aside in the court of its rendition. As this plea was based upon an adjudication under the reorganization provisions of the Bankruptcy Act, effect as *res judicata* is to be given the federal order, if it is concluded it was an effective judgment in the court of its rendition. The problem before the Supreme Court of Illinois was not one of full faith and credit but of *res judicata.* In this particular case, a federal question was involved. This was the power of the federal courts to protect those who came before them relying upon constitutional rights or rights given, as in this case, through a statute enacted pursuant to constitutional grants of power."

In the instant case the respective classes of stockholders of the debtor, R. Hoe & Co., Inc., the common stockholders as a class and the A stockholders as a class, relying upon rights given them through the bankruptcy statute enacted pursuant to constitutional grants of power, agreed among themselves as to their respective rights in the future to amend the charter of the debtor and to ultimately take over control of Hoe. This, it has been held, is a judgment *in rem* binding upon the debtor corporation and upon all of its stockholders past, present and future.

The Supreme Court of the United States said, in the case of *Gratiot County State Bank* v. *Johnson,* 249 U. S. 248:

> "The adjudication is, for the purpose of administering the debtor's property, that is, in its legislative effect, conclusive upon the world * * *. So far as it declares the status of the debtor even strangers to the decree may not attack it collaterally * * *. But an adjudication in bankruptcy like other judgments *in rem* is not *res adjudicata* as to the facts or as to the subsidiary questions of law on which it is based, except as between parties to the proceeding or privies thereto."

In the case of *Durant* v. *Abendroth,* 97 N. Y. 140, the Court of Appeals of the State of New York, said:

> "So far as the estate of the petitioning bankrupt is concerned, the proceeding is in the nature of a proceeding *in rem* and when the *res* is brought before the Court its adjudication is binding upon the interests of every person whomsoever in that *res.* All persons interested therein must follow it and assert their rights, or be debarred. * * * The general rule as to proceedings *in rem* is that when the property is within the jurisdiction of the Court pronouncing judgment, whether domestic or foreign tribunal, whatever the Court settles as to the right or title or whatever disposition it makes of the property is valid in every country."

It has been held that not even the Bankruptcy Court, making the order has jurisdiction to modify it, or the plan approved thereunder. See *In rem Tom Moore Distillery Co.,* 52 Fed. Supp. 938; *Re Argyle Lake Shore Corp.,* 98 Fed. 2d 372; *Re Corona Radio & Television Corp.,* 102 Fed. 2d 959 (7th Ill. C.C.A.).

That the Court which originally made the order in the 77B proceeding did not have jurisdiction thereafter to

modify the rights of the parties or to amend the plan so as to change rights which were vested thereunder, has been held in the case of *Re Diversey Bldg. Corp.*, 141 F. 2d 65, 55 A.B.R. (N.S.) 716 (144; C.C.A., 7th Ill.). Sparks, Circuit Judge, said in the *Diversey* case:

> "We cannot accept appellant's interpretation of sub-section (f) of this Act. We are convinced that Congress did not intend that a debtor-corporation should be permitted to ask for a radical change of plan of reorganization after it had been confirmed by the Court and was being executed under the Court's supervision. It is quite true that the quoted language from sub-section (f) states that changes and modifications may be proposed before or after a plan is confirmed; however, this sub-section must be construed with other pertinent sub-sections, such as (g) and (h), in determining the intention of Congress. *Here the plan as confirmed had been in operation for almost eight years, without complaint so far as this record shows, and it was originally proposed by the debtor itself. Under these circumstances we think the Court was without jurisdiction to entertain appellant's motion. We interpret sub-section (f) to mean that changes and modifications after the plan is confirmed refer to such changes as will better aid in carrying out the plan which has been finally confirmed, and not such changes or modifications as will materially alter the property rights established by the decree of confirmation, and in no event shall any change be made without the consent of the Court.*
>
> "In support of its contention, appellant relies on *In re H. W. Clark Co.* (C.C.A. 7th Cir.), 79 F. 2d 681; *Downtown Invest. Asso.* v. *Boston Metropolitan Bldgs.* (C.C.A. 1st Cir.), 81 F. 2d 314, 30 A.B.R. (N.S.) 483; and *In re Celotex Co.* (D.C.), 12 F. Supp. 1. These

cases relate to amendments of the plan of reorganization before its consummation, and for that reason we think they are not in point. We find no authority supporting appellant's interpretation of sub-section (f). Carried to its ultimate conclusion we think it would end in confusion worse confounded both for the creditor and the debtor.

"Appellant urges that the decree of June 28th, 1935, was not a final decree in that the case was not finally disposed of. That decree, however, was interlocutory in its character, and definitely fixed all the rights of the parties, and it was a final and appealable decree. True, the terms of the trust indenture were not fully performed, and, indeed, full performance could not be required until 1950. However, *the property rights were fixed,* there was no failure of performance on the part of the debtor and its guarantor, and there was no indication that there would be such failure until the principal of the debt was due. Under these circumstances we think that neither the debtor nor the Court could alter those property rights as fixed by the interlocutory decree."

"The district court did not indicate the basis for its ruling. However, we think it was without jurisdiction to grant the relief prayed for."

Summarizing the foregoing orders of the U. S. District Court for the Southern District of New York, and the law applicable thereto in the enforcement of those orders, we arrive at the following conclusion: The debtor-corporation, R. Hoe & Co., Inc., in order to be discharged from the 77B proceeding, had to have the consent of two-thirds in number and amount of its creditors and each class of its stockholders affected by the plan of reorganization. By the plan of reorganization finally approved, control of the

corporation passed to the Class A stockholders, they having the right to elect nine out of the eleven directors while the common stockholders had the right to elect two directors. This situation was augmented by an additional provision which gave the common stockholders the right to vote only on the proposition of dissolution and not to vote upon the proposition of consolidation; but such limitations on the rights of the common stockholders to vote were provisional and the provision is incorporated in the plan of reorganization as follows:

> "provided, however, that after all accumulated and unpaid dividends on the Class 'A' stock are paid in full through the last quarterly dividend period and thereafter so long as the Company is not in default in four or more quarterly dividends on the Class 'A' stock (whether consecutive or not), the Common Stock, voting as a class, shall have equal rights with the Class A stock, voting as a class, on all matters other than the election of directors; and provided, further, that except with the consent of a majority of the Common Stock, no amendment of the certificate of incorporation shall be made which shall impair the right of the Common Stock voting as a class to elect and continue in office two members of the Board of Directors as such Board shall be constituted from time to time, or which shall impair the class voting rights of the Common Stock on matters other than the election of directors conferred upon it by the foregoing provisions of this sentence."

The A directors being representatives of the Federal Court were fiduciaries in respect to the common stockholders. Though the common stockholders were the owners of Hoe, the Bankruptcy Court placed the A stock-

holders in temporary control as its representative, to protect their investment. The temporary control was given to the A stockholders not as owners but as trustees. Their tenure was specifically defined and was to end as soon as their arrearages were paid. That was clearly the intent of the bankruptcy reorganization and was followed for many years.

The present group of A directors took office pursuant to that reorganization plan and as trustees for the Bankruptcy Court in 1946 when the preferred stock was eliminated. Their trusteeship was similar to a spendthrift trust in which the beneficiary (the common stockholders) is protected until he reaches a sound financial position (arrearages paid off). In establishing this trust and depriving the common stockholders of many of their rights of ownership during its existence the Bankruptcy Court did not grant power to the trustees to extend its duration—at least not without the consent of the common stockholders. Nevertheless, that is exactly what the A stockholders have accomplished here. Not only have they extended the duration of the trust but they appropriated much of the beneficiary's interest therein.

Ordinarily, trustees who appropriate the beneficiary's interest for their own use are guilty of despicable crimes. The A stockholders and directors as trustees have done the same thing here, but because they have covered their criminal act with a cheesecloth (the consolidation) the Trial Court and the Appellate Division not only did not consider it a crime but held it to be perfectly legal.

This Court should not permit itself to be blinded from the true facts and should recognize the gross breach of fiduciary duty of the A directors.

Since the decrees in the Bankruptcy Court are *res judicata* in the State Court, the provisions thereof are in

full force and effect, assuring the common stockholders the right to vote cumulatively as a class upon all matters other than the election of directors as well as upon the amendment of the certificate of incorporation.

The plaintiff was entitled to a judgment on behalf of the common stockholders declaring that the action of the Class A directors and stockholders violated a vested property right of the common stockholders contained in the decrees of the United States District Court; that the decrees of the District Court upon the basis of which the debtor, R. Hoe & Co., Inc., was discharged from bankruptcy are binding upon the debtor and the respective classes of stockholders and their privies.

POINT IV

This Court should pierce the corporate veil of "the recently formed" dummy, Hoe Export-Import Corporation, disregard its form as a subsidiary, and regard it in substance as an instrument or device conceived and created, by the Class A directors of R. Hoe & Co., Inc., for the sole purpose of the evasion of the law which gives the common stockholders the right to vote upon the proposed reorganization.

Sections 35, 51, Stock Corporation Law;
Wormser, The Disregard of the Corporate Fiction and Allied Corporation Problems, pages 63-65;
Small v. *Sullivan,* 245 N. Y. 343;
U. S. v. *Lehigh Valley R. R. Co.,* 220 U. S. 257;
Northern Securities Company v. *U. S.,* 193 U. S. 197;
Stockton v. *Central R. R. Co.,* 50 N. J. Eq. 52.

This subject is treated rather fully in Wormser's "Disregard of the Corporate Fiction and Allied Corporation

Problems" on pages 63 to 65 inclusive, where the author says:

> "Oftentimes the corporate form of organization is adopted in an endeavor to evade a statute or to modify its intent A forceful example is to be found in the learned decision of the United States Supreme Court disregarding the theory of corporate entity in enforcing the 'commodities clause' of the Hepburn Act. (*U. S.* v. *Lehigh Valley R. R. Co.* [1911], 220 U. S. 257, 31 Sup. Ct. 387 [per White, C. J.]). The commodities clause provides that:
>
> "'It shall be unlawful for any railroad company to transport from any State * * * to any other State * * * any article * * * manufactured, mined or produced by it, or under its authority, or which it may own in whole or in part, or in which it may have any interest, direct or indirect * * *.'
>
> "The government, in the first suit, alleged that the Lehigh Valley Railroad Company owned stock in a coal company whose goods it was carrying. On demurrer, it was held that no violation of the statute was thereby shown; the court interpreted 'interest, direct or indirect' as meaning only a legal or equitable interest in the transported articles. (*U. S.* v. *Delaware & Hudson Co.* [1909], 213 U. S. 366, esp. 413.) The government, after this first and very serious blow, presented an amended complaint in which it was set forth, in addition to the allegations of the prior complaint, that the railroad company was using the coal company merely as a sham, a device and a dummy, in order to evade the provisions of the act.
>
> "The court held that no such evasion could succeed, and, disregarding the corporate concept and looking at the substance and reality of things, decided that it was within its jurisdiction to issue an injunc-

tion. (1911, 220 U. S. 257, *et seq.*) It is submitted that every dictate of sound reason warranted the court in holding as it did.

"The late Justice Brewer in his notable concurring opinion in *Northern Securities Company* v. *United States* (1903), 193 U. S. 197, 360-4, pointed out that, where a corporation was organized merely as a convenient means of combining separate railroad properties under one control the court could shake aside the veil of entity and regard the combination as just 'as direct a restraint of trade by destroying competition as the appointment of a committee to regulate rates.' In other words, the plain intent and purport of the Sherman Anti-Trust Act cannot be defeated by a resort to the sham and subterfuge of incorporation."

It is clear that the formation of Hoe Export-Import Corporation is a patent fraud not only upon the common stockholders but upon the corporation itself, and that the evasion of the law cannot be countenanced even when it is done by quasi-legal means.

In the words of the late Chancellor of New Jersey, in *Stockton* v. *Central R. R. Co.* (1892), 50 N. J. Eq. 52, 75-6:

"'* * * A more flimsy device, when the particulars are once known, it is impossible to imagine. It may succeed for a time in baffling persons. * * *' It must not be thought that courts are powerless to strip off disguises that are designed to thwart the purposes of the law. The mere suggestion of such a condition is an insult to the intelligence of the judiciary. Whenever such disguises are made apparent, they can readily be disrobed. The difficulty is in showing the disguises, not in penetrating them when they appear."

POINT V

There is a question of substantial public importance presented by this appeal and the motion for leave to appeal should be granted.

Respectfully submitted,

GUSTAVE B. GARFIELD,
Attorney for Plaintiff-Appellant.

Extract from Certified Copies of the Respondents' Brief at the Court of Appeals (p. 58 thereof) showing its Summary of Federal Question.

"POINT VII

THERE HAS BEEN NO VIOLATION OF THE FEDERAL COURT ORDERS.

In his brief Katz argues that this consolidation violates the plan of reorganization approved by the Federal Court in the Hoe 77 B proceeding of 1935—or, to state it differently, that the certificate of incorporation, as amended and approved by that court when the debtor was discharged in 1935, immutably defines the rights of the stockholders; and cannot later be amended or altered in any respect or by any means. To state the claim is to answer it.

Both lower courts and the Federal courts have dismissed the contention as unsound; and it is worthy that Katz' colleague, Martin, does not say one word in support thereof."